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UNIVERSITY OF ALBERTA

MARKET SOCIALISM IN EASTERN EUROPE

BY

ELAINE B. FRANK

A thesis submitted to the Faculty of Graduate Studies and Research in partial fulfillment of the requirements for the degree of Master of Arts.

DEPARTMENT OF POLITICAL SCIENCE

Edmonton, Alberta
SPRING, 1992

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Elaine Frank

Elaine B. Frank
Box 433
Southey, Saskatchewan
S0G 4P0

April 5, 1992.

UNIVERSITY OF ALBERTA

FACULTY OF GRADUATE STUDIES AND RESEARCH

The undersigned certify that they have read, and recommend to the Faculty of Graduate Studies and Research for acceptance, a thesis entitled **Market Socialism in Eastern Europe** submitted by **Elaine B. Frank** in partial fulfillment of the requirements for the degree of **Master of Arts** in **Political Science**.

Fred Judson
Fred Judson, Associate Professor

Charles Nunn
Charles Nunn, Assistant Professor

Laurie Adkin, Assistant Professor

April 29, 1992

For mom

dad

Kevin

Glenda

Sandra

Christina

Daryl

Alicia

ABSTRACT

Currently, East European states are attempting to promote economic and political decentralization. Politically, the desired end is "democracy". Economically, decentralization does not necessarily imply that capitalism will evolve or is even the desired end. This essay does not question the need for stabilization and marketization in Eastern Europe; but, instead considers how best to promote these ends. There are two basic economic strategies that East European countries can promote: a rapid or a gradual marketization strategy. The former is based on a liberal or orthodox economic analysis and it prescribes a rapid and comprehensive approach combined with a restrictive fiscal and monetary policy. The intent or hope is to induce the formation of a capitalist market and to promote international economic integration. This essay will demonstrate that an orthodox economic analysis and its prescriptions are limited and would lead to failure because social and political factors are not considered or included.

The alternative, a gradualist strategy, is vague and uncertain. This strategy focuses on domestic maturity and would lead to a dual economy if successfully promoted. Such an economic structure could be considered market socialist. This essay will develop the economic limits which suggest that market socialism may yet have a future--at least in Hungary. Moreover, there is significant political support in Hungary for an alternative development strategy. It is wrong to suggest that Hungarians have transformed en masse into capitalists, and, more generally, that capitalism is around the corner in Eastern Europe.

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INTRODUCTION

I. FANFARE AND REALITY: ECONOMIC DEVELOPMENT CHOICES

The initial euphoria over the "triumph of Western political democracy" and the capitalist economy in Eastern Europe has abated somewhat since the exciting events of 1989.(1) Recognition has grown that smooth, harmonious economic and political transformations are unlikely.(2) Prices, unemployment, job insecurity, and poverty are all on the rise. In 1990 in Hungary, for example, the poverty line was estimated at 6300-6500 forints per individual, and 22-23% of the population lived below this line.(3) The average wage currently in Hungary is approximately 10,000 forints per individual and the poverty line is expected to increase to 8,000 forints in 1992.(4) The seeming ease of the political changes in Eastern Europe in 1989 led many analysts to believe that the political and economic transformations following the collapse of Communism would also be relatively rapid and painless. Economically, stabilization and privatization policies would induce, without major impediments, the development of a capitalist market. Politically, the strength of social mobilizations in toppling the Communist regimes suggested that an active, democratic political culture could be found in the East.

The collapse of Communist political power occured in the midst of a severe economic crisis. Indeed, economic crisis was a central factor precipitating the decline of Communist power. In Hungary, for instance, as Stark and Bruszt summarize:

> The promise of compromise [made by the Communists to institutionalize power sharing] issued not from some surge of fresh optimism following the May 1988 ouster of Janos Kadar and his retinue from the pinnacle of the Hungarian Socialist Workers Party (MSzMP), but from a growing sense of foreboding crisis. Hard-liners, party reformers and independents--who, it should be emphasized, had not yet coalesced into an "opposition"[compromise with the present regime--rather than confrontation--was still viewed as possible]--shared a basic perception of the situation: Left unchecked, the widening scope and quickening pace of Hungary's downward spiral into economic, social and political crisis could lead to chaotic threats to the social order.(5)

Economic crisis played an important role in promoting political change, and the ability or inability of new regimes to deal effectively with economic difficulties will affect the evolution of political and economic institutions in Eastern Europe. Economic stagnation coupled with the dislocative effects of economic transformation will make basic survival a priority for most peoples in Eastern Europe. Richard Bruner writes,

> Many Hungarians cope by tuning out. A recent survey of Hungarian adults revealed that 39% of Budapest residents do not read any of the many national and local newspapers (the same is true of 30% of the entire country). . . . People are simply tired of politics . . .
>
> . . . most Hungarians are concerned with survival, inflation, and having enough money for food and everyday needs . . . . There's a lack of interest or trust in the present and future . . . apathy . . . inhibits the positive benefits of what the democratic process and democratic action can yield.(6)

Because of the central role of "economics" in shaping the future of Eastern Europe, the focus of this essay will be primarily the economic aspects of change. An economic focus, however, does not deny the relevance of political factors such as the development of political parties and intermediary social interest groups, or the reasons for and implications of the political institutional changes already made.

Because of economic similarities between East European states, a general analysis of various economic policy options is possible and valid. There exists a strong consensus in Eastern Europe that stabilization, marketization, and privatization must be promoted--differences lie primarily in how to promote the above. The need for stabilization and marketization (hence privatization) is not disputed, instead this essay will consider the effects of different economic policies. Fundamentally, economic policy can be categorized under either "rapid" or "slow" marketization approaches.(7) A rapid marketization approach relies largely on foreign capital and aims for international economic integration. It urges rapid privatization with minimal concern about "who" the future owners are--its end is to dismantle the state sector as quickly as possible. Doing so, it is argued, induces the formation of a capitalist market, in turn, allowing it to perform its "allocative-efficiency" magic. Further, because of the emphasis on speed, it is the state-owned enterprises that are most successful or profitable that are sold (primarily to foreign capital as there is a dire lack of domestic capital). A rapid privatization approach also emphasizes stabilization through restrictive fiscal and monetary policy, and calls for the immediate implementation of "real" prices (or for a complete and rapid elimination of subsidies).

A slower marketization approach--euphemistically referred to as the "Third Way"--takes into account the social and political factors which affect and limit economic policy, and its primary objective is to promote the development of a domestic bourgeoisie.(8) Gradualism is necessary as it will take time for a national bourgeoisie to form (and then take control of state-owned assets). Third way advocates do not believe that there are great benefits to be gained in the rapid dismantling of the state sector. Instead reregulation of the state sector and deregulation of the private sector are argued to be the most propitious means for ensuring present stability and in promoting future goals. Marketization is viewed as a long term process that cannot be artificially created or stimulated. Since the goal of this strategy is to promote the formation of a "middle class" its fiscal and monetary policy is necessarily less restrictive than that of a rapid approach. The focus of a gradualist strategy is domestic maturity rather than international integration.

Although the aims of these two approaches are generally the same (marketization and stabilization), the different means imply very different ends. This essay will argue that a rapid marketization policy would fail and, moreover, would lead to economic calamity. A slower marketization policy does not guarantee success; yet, it is a safer gamble then a radical economic revolution and its impact on the present generation of East Europeans would be less onerous. Furthermore, if a third way policy is pursued then the evolution of "market socialism" in Eastern Europe is a possibility. Arguments that "socialism" has been mortally wounded are inaccurate. Liberalization has different connotations in the East and it is not as widely embraced as Western rhetoric tends to suggest.(9)

The implications of this analysis are viewed as generally applicable to Eastern Europe; but, it must be stressed, domestic political conditions will determine the economic policies ultimately pursued. To move away from economic generalizations and to consider some political elements of the transformation, special attention will be given to Hungary. A case study will be made of Hungary for several reasons. First, Hungary has had a history of reform. Indeed, the New Economic Mechanism (NEM) of 1968 was an attempt to create market socialism.(10) This attempt failed, and although it points to many problems and tensions of such a system, it is too glib simply to dismiss market socialism as an unviable alternative. A major hindrance to successful economic reform was the continued centralization of political power in Hungary. The purpose of the NEM was to decentralize the economy, but there was no parallel intention to change Hungary's political structure.(11) Second, Hungary has a relatively developed private sector suggesting that the promotion and evolution of a market should be, compared to other East European states, relatively easy.(12) Finally, there is a great deal of information on Hungary, written by Hungarians--particularly on questions of political economy.

II. THE CENTRALIZED MODEL

The following brief history of the centrally planned economies illustrates the reasons for the current economic crisis, and the economic institutional structure that the new regimes have inherited.(13) Brus uses the term "centralized model" to depict the Soviet and East European economies and lists the following five features as basic to the centralized model:

1. The concentration of practically all economic decisions on the central level (except for individual choice in the fields of consumption and employment);
2. The hierarchical nature of plans and the vertical links between different parts of economic apparatus;
3. The imperative form of transmitting decisions downwards;
4. The predominance of economic calculation and planning in terms of physical units; and,
5. The passive role of money within the state sector.(14)

To this list Ellman adds political dictatorship and a mono-hierarchical system.(15) Economically, the salient feature of the centralized model is that the allocation of resources is made vertically rather than through horizontal market exchange relations. The articulation of information within a system dominated by vertical relations is done primarily in physical quantity terms. Because the central plan is based on physical quantitites, state enterprises are also quantity-oriented: not money-, price-, or cost-oriented, as in horizontal market relations. The result, argues Ellman is "the (normal) absence of competition and the dominant role played by the fulfilment of evaluation criteria imposed from above, rather than use criteria insisted on by customers."(16) Rather than develop a step by step analysis of every problem, the example of management behavior, developed below, illustrates many of the problems found in the centralized economies.

First, the selection of managers rests largely on the principle of partymindedness:

> The principle of partymindedness means that the [economic] plan is a concrete expression of party policy. It must look at all problems from a party standpoint. This principle is of great importance in all the state socialist countries. A major reason why economic reform proved abortive in the USSR in the 1960s [and in Hungary in the 1970s] was because, as one State Planning Commission official put it (Krylov 1969), "in practice it means a weakening of the role of the socialist state and the party of the working class in the management of the economy." The partymindedness of planning is ensured, interalia, by party control over appointments and promotions.(17)

Management's main objective is to meet quantity targets established from above, and it is primarily concerned with fulfilling the current target not with future performance.(18) The results of this are, first, little or no incentive to innovate or reorganize the labour process. Indeed, the incentives promoted by this system tend to work in the opposite direction: managers are rewarded for meeting current targets; hence they are likely to avoid incorporating new techniques that may prevent fulfilment of the short-term target, but would improve long-term performance. The problems of outdated production techniques and inefficient organization are in large part due to the very risk-averse behavior of managers. Second, the emphasis on physical indicators, or on maximizing quantity, leads to, for instance: large (usually undisclosed) input stockpiles (to ensure current target fulfilment as input suppliers are not dependable and because the centralized economy has been plagued by shortages); and, minimal concern with quality. Third, although the goal of management is to meet the target, it also plays a role in setting the target. To ensure that the target is met, management, for example, will tend to underestimate its productive capacity and to overestimate its required inputs. The informational problem for the center is a mammoth imbroglio without receiving inaccurate or distorted information from its parts. (Imperative planning is often perceived as the major culprit and its replacement with indicative planning was an important element of the 1968 reform attempt in Hungary.)

The extremely risk-averse behavior of management, rational within centralized economies as indicated above, leads to a fundamental problem for these economies: lack of innovation and restructuring. In a capitalist economy, finance capital supports the innovation and restructuring of industrial capital. Finance capital, or credit, facilitates the movement of surplus value from dying or shrinking capitalists to growing capitalists, and has played a key role in the competitive selection process of the capitalist market. The centralized model gives a passive role to money and prices, but it has not developed an alternative means to induce innovation and adaptation. Kornai's analysis of a hard versus soft budget constraint is also relevant to this problem.(19) State enterprises have targets to meet, yet there are no real constraints (that is, bankruptcy and closure) placed on them. The soft budget constraint prevents the natural selection process that the market, with its hard budget constraint, induces. The market (theoretically) weeds out the inefficient and unprofitable, with finance capital acting as an important vehicle to support the time necessary for innovation. In a centralized economy the state bails out every firm, without discrimination, eliminating any inducements to maximize efficiency, develop new technology, etc. In 1980, Kornai wrote,

> During the first ten years of reform in the Hungarian economy practically no bankruptcy occurred: no firm operating with losses was fully liquidated. Workers are guaranteed not only employment, but even employment in their present jobs. Following the price explosion on the world market not a single Hungarian firm went bankrupt. Using the popular expression in Hungary: the state budget "took over" the losses. The "natural selection" entailed by economic competition did not take place: the strong and the weak, the active and the passive, the innovative and the incompetent all survived the storm.(20)

One important characteristic exhibited by all the centralized economies was the shortage economy or the sellers' market.(21) Regarding consumer goods, the wellpublicized outcome of the shortage economy was long queues, while in the producer goods sector, customers were limited in their ability to bargain freely with suppliers. The shortage economy tends to exacerbate the microeconomic problems developed above, for example, production that is not based on customer criteria or for use. Moreover, a shortage economy tends to perpetuate itself (adjustment does not entail a simple step to a new equilibrium point). One important reason for the continuation of the shortage economy, however, had been the tendency of the centralized economies to adopt over-ambitious plans, exceeding the resources available.(22) "Economic growth" typically had been treated as an end in itself by the centralized economies--without concern for the economic distortions that over-rapid growth can produce. The myopic focus on growth led to wasteful overinvestment and overconcentration of investment in the producer goods sector.(23) Overinvestment led to structural bottlenecks (input constraints such as the lack of qualified labour). Input shortages and structural bottlenecks often resulted in lengthy delays of project completion and in the "waste of resources in uncompleted investment projects."(24) Moreover, lengthy completion times often rendered technology obsolete by the time it was operational.(25)

Another characteristic of the centralized economies was "investment hunger".(26) This describes a situation which evolves because of the lack of objective economic returns criteria for investment and the absence of the threat of bankruptcy. Investors (enterprises, ministries, etc.) do not have economic efficiency as a central goal. Instead, given the nature of the system, their motivation is primarily to increase their political power and greater access to investment funds is one way of achieving this. Related to the problem of investment hunger is what Ellman calls "departmentalism".(27) Ministries compete for investment funds, view the interests of their own sector as primary, and tend not to cooperate with each other or to consider the interests of the economy as a whole. By increasing the power of one's "department", one's own power is also increased. The centralized model was not successful in promoting social over particular interests--an important socialist goal and a central element in its critique of capitalism.

The above survey is incomplete yet it provides an outline of many of the problems inherent in the centralized model and illustrates the reasons for current economic difficulties--a characteristic shared by East European countries. Major problem areas for all of the East European states can be grouped as follows: "a structure of production dominated by heavy industries, an unusually high energy and material intensity of production, distorted factor and product prices, an old and often obsolescent capital stock"(28); a neglected infrastructure; difficult readjustment as a result of collapsed intra-CMEA trade (all Eastern states have been adversely affected by rapidly declining intra-CMEA trade--in Hungary, for instance, in 1989 its export and import growth rates to Eastern Europe were -2.7% and -6.6% respectively, and in 1990, -24.6 and -8.6)(29); "large foreign debts, the servicing of which would require the transfer of 3-5% of GNP [for Hungary, Poland, and Bulgaria] to the West"(30); serious environmental degradation; and "increased open or suppressed inflation, shortages and interruptions to supply that are not being corrected"(31). Dealing with this quandry is a Herculean task with no easy or obvious solutions.

Despite Hungary's history of economic reform, its economic performance has not been superior to other East European economies.(32) Comisso and Marer write,

> . . . while the economic objective of the NEM was to improve efficiency and performance, its political rationale was improving central control and coordination of economic behavior.(33)

The limited and indeed contradictory nature of the NEM meant that it was incapable of inducing a change in state-owned enterprise behavior. The most salient changes that the NEM introduced in the state sector were the shift from direct to indirect planning and the abandonment of physical targets (indicative planning replaced imperative planning, allowing greater enterprise autonomy).(34) For state enterprises, market signals such as prices and profits were to be given greater significance as production guides rather than direct commands from above.

The success of the move to indirect planning was, however, limited for several reasons. A main reason was the replacement of the "plan bargain" with the "regulation bargain", hampering the use of market criteria.(35) Berend points out, "the lack of a consistently normative regulation, [and] the masses of exceptions led to the reproduction of central directives by other means of regulation."(36) An economic structure resembling a "market" did not arise in the state sector; instead bargaining, both vertically and horizontally (between state-owned enterprises), remained the norm. The significance and concentration of the state sector meant that many state enterprises enjoyed a monopoly position both economically and politically, leading to exceptions and exemptions which prevented adaptation to market forces. By 1973, "the Council of Ministers in fact took the 50 biggest industrial enterprises" and "placed them under direct central control. These held 60 percent of Hungarian industrial assets, produced approximately a half of the country's industrial output, provided for more then 60 percent of exports and employed 700 thousand men (sic)."(37) The NEM did not improve Hungarian economic performance, nor did it move Hungary, in any meaningful sense, away from the centralized model.(38) The past political structure in Hungary, as will be highlighted in chapter two, prevented economic reform from inducing changes in state-owned enterprise behavior.

III. DEFINITIONS

The radical and dramatic changes in Eastern Europe in 1989 were presaged by years of debate on the meaning of socialism, market socialism, and capitalism. Defining these concepts is no easy task. Often definitions seem to be writer-specific. My purpose is not to disentangle these definitions; but to elaborate on how they will used here. Capitalism and socialism will be treated as broad categories. Within these categories different types are viewed as possible (under capitalism different varieties are found, for example, in Japan and the U.S.). Under socialism, there was "actually existing" socialism, and theoretically numerous varieties are elaborated and defended.(39) There is not a socialist model. The socialism that this essay considers is market socialism.(40) Although rapid liberalization is rejected as a propitious alternative, the need for a market is not (capitalism is not synonymous with market). The issue is what type of market; what is the role of the market; or, what is the role of the private sector under (market) socialism? Part of the definitional problem is that these terms (market, socialism, etc.) are loaded with subjective and/or ideological connotations. Brus argues:

> There are no theoretical foundations for worshipping administrative directives as a synonym for planning, or for idealizing the market mechanism as a synonym for harmony with the requirements of objective economic laws, particularly for the law of value. There are no theoretical grounds for denying that requirements of objective economic laws can be achieved through direct commands, or for denying that planned targets can be reached through the market mechanism. In particular the theory of a regulated market mechanism--strongly attacked on doctrinal grounds--in itself contains nothing that would make it alien to socialism or basically inconsistent with the premises of a socialist economy.(41)

IV. CONCLUSION

This essay will consider the different options open to East European countries in their attempts to transform their economies and to abate the current economic crisis. The need to promote marketization is not disputed--what is considered is how marketization is promoted. The first chapter examines the likely consequences of a rapid marketization policy and argues that such an approach would fail to realize the aims of its advocates (a capitalist market would not result), and it would debilitate these economies. To prevent economic collapse while forwarding marketization, a gradualist, centrally-controlled strategy is needed. Moreover, a deliberate and gradualist policy may lead to the evolution of an economic structure that could be considered socialist (market socialist). The second chapter examines why this may be the case; defines market socialism and discusses why a "market" is necessary; and, considers some criticisms of market socialism. The final chapter will speculate on political and social limits and possibilities for market socialism in Hungary. It demonstrates that a major obstacle to the promotion and development of market socialism is simply political apathy--not lack of "political" debate about an alternative development model, but lack of "public" debate.

There are no easy answers or uncontradictory solutions for Eastern Europe. Further, the enormity of the economic restructuring task that it faces cannot be exaggerated. Comisso writes:

> One way of conceptualizing the nature of the problems, opportunities and choices confronting the countries of East Central Europe is to imagine what would happen if

> the United States were suddenly transported intact to another planet. In the economy, traditional trade links would be cut and terms of trade altered, and formerly strong industries and firms would lose their markets, since much of their output would be either obsolete or unable to be manufactured due to a lack of raw materials. Skills would be depreciated, and natural endowments and comparative advantages would have to be reevaluated in light of the new international environment. Politically, as well, Americans would have to decide whether to create institutions compatible with a new planetary order, or whether to retain popular but perhaps poorly adapted features of their own political traditions in order to keep some semblance of life on Earth intact as people adjusted to new conditions and expectations.(42)

This analogy may seem fantastic, but it does indicate the nature of the difficulties that East European states must deal with. What we are likely to see in response to these new challenges is a combination of rapid and slow approaches and it may often seem that no policy at all is evident.(43) The following analysis attempts to highlight the least painful and most beneficial economic policies for the present and future generations of Eastern Europe.

CHAPTER ONE: ECONOMIC CATASTROPHE AS REVOLUTION

This chapter will examine the suitability of rapid liberalization policies for East European states as they attempt not only to transform their economies (from centrally planned to market), but also to assuage current economic difficulties. Initially, I will consider the arguments forwarded by Jeffrey Sachs, an influential Harvard economist and top Western advisor to East European countries, in his article "Eastern Europe's Economies: What is to be Done?".(1) Sachs's arguments that the transition must occur rapidly and comprehensively are widely accepted in the West and East as the appropriate road for East European states to follow.(2) Further, Sachs's analysis is representative of mainstream or orthodox economics and this chapter, although it focuses on Sachs, is an implicit critique of orthodox economic analysis and policy prescriptions.(3) This chapter argues that rapid transition policies, which prioritize international economic integration, hinder domestic development and would fail to bring about a functioning, Western-style capitalist economy.

I. STABILIZATION

Sachs lists the following four elements as central in his (how to make a market) policy proposal for East European economies:

(1) A policy that induces prices to move to their market clearing levels;

(2) Reform (commercial law and tax) to spur the growth of the private sector;

(3) Policies to either privatize (the focus) or discipline the state sector; and,

(4) Restrictive credit and balanced budgets to maintain macroeconomic stability.(4)

Two other elements stressed in Sachs's proposal are the need for the above to be promoted simultaneously, comprehensively and rapidly (to induce the development or formation of a market); and, it gives (and requires) a major role to Western assistance (to finance the social safety net needed to provide some relief and security to those adversely affected by the transition).(5)

The first element--market clearing prices--necessitates free trade, currency convertibility, and complete elimination of price controls and subsidies (for both consumption and production goods). In other words, Sachs's policy calls for the immediate imposition of hard budget constraints. The implications of this policy are: a sharp currency devaluation; rapid price increases; closures; and, a surge in unemployment. Market clearing prices, restrictive credit, and balanced budgets are necessary and must be achieved as soon as possible, argues Sachs, because "sensible prices are vital for efficient resource allocation."(6) Furthermore, sensible prices will indicate which state enterprises suffer chronic losses and are ripe for closure. Although the transition induced by the above economic policy will not be easy, Sachs declares that "Western observers should not overdramatize lay-offs and bankruptcies. Poland, like the rest of Eastern Europe has too little unemployment not too much."(7) Or an "efficient" labour market, for Sachs, implies that unemployment is necessary: too little unemployment leads to a soft, lazy, and costly labour force.(8) Finally, continues Sachs, "A growing private sector will absorb workers; the profitability of firms will provide an accurate guage as to which ones should be closed; and a social safety net will be established by Poland in 1990."(9) All the pieces fit in Sachs's blueprint: the elements of his proposal harmoniously reinforce each other and any workers negatively effected by the transition and not reabsorbed will be protected by a state funded social safety net.

Sachs does not relate the economy to political or social institutions. Consequently, Sachs promotes and believes in the effectiveness of a narrowly economic policy approach.(10) His policy induces economic hardship, for example, but he simply dismisses this as unimportant (even necessary). However, what is to happen to the large number of individuals who will be negatively affected by such rapid change? How long will it take for a market to form (if it does at all) and reabsorb those tossed out by the transition? How will individuals react to such upheaval? The individual that Sachs describes is a passive character who will quietly await reabsorption. Political and social limits are not accounted for in Sachs's policy. How will workers react to closure and unemployment? The idea of a labour market that will eventually induce corrections may not be as easily accepted by workers in the East as compared to Western labour. It is important to remember that "equality" and "employment guarantees", for example, were more than ideological baggage that vanished in 1989. Although the ideological elements of socialism should not be over-stated, it is just as foolish to believe that these principles are now meaningless for the peoples of Eastern Europe. Further, although a social and political consensus for change to a market economy may currently exist, this does not imply that this consensus can be sustained--as the costs of the transition mount, reversals in policy are not unlikely. The need to maintain political and social consensus is likely to conflict with Sachs's requirement of a rapid and comprehensive transition: the more rapid the change, the more negative the social consequences (for example, rising unemployment and prices), and the more likely opposition is to rise.(11)

Sachs's proposal emphasizes restrictive monetary and fiscal stabilization policies, and then pulls in Western assistance as a _deus ex machina_ to solve social problems created by too rapid economic change. The none-too-radical

Secretariat of the Economic Commission for Europe summarizes,

> The transition to the market economy will inevitably involve painful changes. Any foreseeable level of foreign assistance will only be able to reduce this burden slightly, so that the costs of the transition will mainly have to be absorbed by the peoples themselves.
>
> What is more, there is no guarantee that the reforms will succeed. This uncertainty applies particularly strongly to any estimates of the social costs of the transition and reinforces the need for wide social backing for the reform programme. Otherwise, unforeseen setbacks could quickly lead to calls for the whole market economy policy to be reversed.(12)

Sachs's proposal requires Western assistance but gives no consideration to the possibility that a Marshall Plan for Eastern Europe may not evolve. Sachs emphasizes that the West must: make "a commitment to incorporate the East Europeans into a common European market"; remove technological export restrictions to the East; and, provide long term financial support (aid not loans).(13) Sachs argues that,

> The most fundamental support needed is a commitment to incorporate the East European countries into a common European market. Western Europe must be prepared to accept new imports from it. That means in agriculture as well as manufacturing; pig

> farmers in the EC will just have to accept that free trade in Polish hams is a price to be paid for living in a united and democratic Europe.(14)

Whether or not the pig farmers or the EC generally will promote quickly (or even slowly) a common European market is questionable.

Longworth writes,

> E.C. policy toward Eastern Europe is evolving slowly. It appears to rule out massive aid along the lines of a Marshall Plan. The Commission instead believes that the East European countries must reform their own economies, but it wants to offer whatever Western help will be useful. It also believes that money is important, but that other things--management training and open markets, for instance--can help even more. But since it sees these changes as a long-term process and refuses even to contemplate E.C. memebership for the East Europeans . . . (15)

In other words, assistance will not be of the type that Sachs hopes for--it will not include large amounts of aid in terms of money. Management training may be important, but Sachs's rapid transition policy will require more substantial assistance. The EC's belief that open markets would benefit the East may not be reflected in its actions as its rhetoric will be tempered by domestic political restraints (for instance, pig farmers), and by the dismal state of the East European economies themselves. There is a limit to how much Western Europe will be willing or able to subsidize Eastern states--change is a long term process and it will take time for these economies to reach a stage where they can offer competitive goods to the West.(16) Deborah Milenkovitch writes,

> ". . . if the European Community were to give the six East Central European nations the same assistance it provides to the depressed regions of Greece, Spain, Portugal, Ireland and Southern Italy, such a level of assistance would amount to $23 billion a year [Delors, 1990]." This would be about five times the size of the Marshall Plan equivalent for the six countries. There is no reason to believe that the countries of East Central Europe will achieve West European levels of development any faster or cheaper than the Marshall Plan beneficiaries did. Indeed, there are many reasons to think it will be slower and more costly.(17)

What kind of aid is the East likely to obtain from the West? Sachs notes that "The West moved rapidly to provide food aid for Poland. But when the Poles asked the World Bank for cash to support workers dislocated at the start of 1990s the bank reacted in slow motion, suggesting that a fraction of the sum requested might be available by next summer."(18) This reaction from the West is not atypical or surprising--no one has come up with a substantial aid package for Eastern Europe. Without substantial Western assistance, given the restrictive, shock-therapy macroeconomic policy that Sachs has prescribed, the East European economic base cannot support all of the following: financing of a social safety net; financing of long term development; and repayment of foreign debt. Even without shock treatment, East European states will find it difficult to cope.

Sachs fails to recognize the gap between the instability that his policy will create and the amount of assistance that will be made available to Eastern states to ease the difficulties created by the transition. Even if Sachs's policy could induce the formation of a market, in an economic sense, social and political tensions from within would limit and most likely prevent its full implementation.(19) Another problem with Sachs's policy proposal is that it will not or cannot induce the formation of a Western-style market. As these next sections will develop, creating a market is not a simple nor merely economic task.

II. MARKETIZATION: PROMOTING ENTRY AND COMPETITION

Sachs is correct in stressing the need for commercial law and tax reform in the private sector. The private sector does have an important role to play particularly in providing consumer goods and services. Commercial law and tax reform, however, will not be sufficient in creating the magic market that Sachs desires. The dominant economic sector in Eastern Europe is the state sector (the state controls approximately ninety percent of Hungarian assets), and this is precisely where the difficulty in reform lies. Sachs's answer is to either privatize or impose financial discipline on the state sector. Privatization will be discussed in the next section, but it is immediately evident that the practical difficulties of privatization of this scale are numerous. Financial discipline is to evolve by allowing competition from foreign imports and domestic private firms (as they emerge).(20)

There has been a great deal of discussion on the problems related to the soft budget constraint (lack of exit); but little attention has been given to the problem of entry. Free entry is important in Sachs's proposal, but how does it come about? Foreign competition is one route, but as Comisso points out this is generally a longer term policy option because of the balance of payments constraint. Comisso writes,

> How much can small countries already saddled with large hard-currency (and ruble!) debt afford to import? Over the long run, the amount would presumably rise as export capacities grow, but in the short run, demand for imports should be expected to be considerably greater than the desired level of supply. . . . The fact that many of Eastern Europe's main industries have a relatively inelastic demand for basic raw materials ("real" prices and "hard" budget constraints would certainly induce some economizing, but the bottom line of a petrochemicals plant is imported oil . . .)(21)

The likely result of a rapid move to free trade would be inflation--with its negative effects on investment, wage demands, etc. Indeed, "an import competition strategy might well tend in the short run to wipe out the very recuperative capacities it is intended in the long run to stimulate."(22) The other point that Comisso raises is that of "inert customers"--the marginal difference in price and/or quality of a foreign supplier may not be great enough to induce a switch to the foreign competitor: the state sector may not be overwhelmed by foreign competition.(23) Supplier transition costs, loyalty, and other political factors may dampen foreign competition effects. If domestic firms prove, however, not to be inert, then there are other distortionary possibilities: "Those firms with access to hard currency (i.e., those that were already competitive on western markets) would be able to choose suppliers; those lacking in hard currency (and hence in greatest need of competition) would be imprisoned within the domestic supply network."(24) In other words, monopoly suppliers could remain monopoly suppliers, and weak companies could remain in a restricted and dependent position.

Another possible problem with the trade liberalization strategy is "whether a rise in the price of inputs will provoke a fall in demand for them; if budget constraints on firms are 'soft', this is not likely to happen, and our socialist economy--now shorn of administrative rationing devices--is likely to start importing goods at an accelerated pace."(25) First, this is an important question because the trade imbalances of the East European countries are due primarily to producer not consumer goods.(26) Second, the negative effects of "neither plan nor market"--that is, the acceleration of imports--have been demonstrated by Hungarian experience.(27) And, third, imposing hard budget constraints is easier said than done. Sachs suggests that this is relatively straightforward: with sensible prices established, those state enterprises which have chronic losses will be shut down. Once subsidies and distortions are eliminated, the market will provide the correct signals. Closure of state enterprises using Sachs's criterion would create a domino effect vis-a-vis state enterprise bankruptcies. Eastern economies are characterized by lateness of payments within the state sector which closely interconnects state enterprises--in Hungary this is known as "queuing enterprises."(28) This problem of queuing is self-perpetuating with each enterprise typically acting as victim (not receiving its payments on time) and culprit (not meeting its payment obligations on time).(29) This cycle is difficult to break. The Secretariat for the Economic Commission of Europe writes,

> A consistent implementation of existing (or planned) bankruptcy procedures would

> 'probably cause more harm than good, as it would lead to a chain reaction throughout the economy.(30)

Sachs's only criterion for closure is profit: loss-makers should be eliminated, along with subsidies, cheap credit, and tax concessions.(31) The difficulty with this criterion, and in simply hardening budget constraints, is that these state enterprises are not starting in a market situation.

> As Tardos argues, simply imposing hard budget constraints on all enterprises in such a context would not only mean mass bankruptcies, but it would mean indiscriminate and economically irrational bankruptcies as well.(32)

The context that Tardos is referring to is the lack of developed labour and capital markets.(33) Hungary, for instance, in its earlier reform attempts allowed product markets but tried to maintain uniform rules in regard to labour and capital allocation.(34) This policy approach (not only political bailouts) also explains why such a large number of exceptions and exemptions resulted: uniform rules are difficult to maintain in practice.(35) Further, as Tardos argues, "there was no feedback to be described by monetary processes between resource allocation and commodity markets, and there was no direct relationship between the resource markets either."(36) Accounting for state enterprises was done on a production cost basis and did not or could not rely on "market prices" because they did not exist.(37) Examining the books of a state enterprise will not be helpful in determining its economic viability. Simply hardening budget constraints is not a sound policy unless developed capital and labour markets are also in place. Sensible prices cannot be established immediately, nor is it automatically evident which enterprises are chronic loss-makers that should be eliminated.

Other problems are defining "sensible prices" and "efficient" resource allocation, and establishing a more-reasoned criteria for closure. Financial discipline and accountability are appropriate economic goals; but arguments to eliminate subsidies, for example, are not based solely on objective economic arguments. Subsidies on consumption and even production goods in no way hinder the operation or development of the market (as is demonstrated by Western experience and current practice). Whether or not we allow the market to make all, some, or very little of our resource allocation decisions is also a political/social issue. Moreover, externalities (which result from allocation decisions made by atomized, self-interested economic actors), for instance, indicate that the market itself does not always lead to the most efficient use of resources from a social standpoint. Another issue related to sensible prices and efficient allocation is the fact that queuing and shortages are different problems than plenty and full shelves with the added condition that many individuals do not have the means to purchase even bare essentials. (Some would view queuing and shortages as preferable.) Both producing and "satisfying" basic needs (food, housing, education, etc.) of an entire populace are arguably worthy economic ends--not only the "efficient" production of those goods.

Another method of creating competition for state enterprises is to stimulate the development of domestic private enterprise. Liberalizing regulations have been effectively used by Hungary in promoting the development of the agricultural sector and the second economy (the first is the state sector). The second economy, however, is predominantly service and consumer goods oriented.(38) The problem is in stimulating domestic producer goods competitors. Again, this requires a more developed capital market, not only liberalizing regulations. Further, as Comisso suggests, "The private-cooperative sector itself is hardly immune to monopoly. In fact, thanks to the climate of uncertainty surrounding private activity in socialist countries to date [1988], individuals have hesitated to start their own business. Those who do take the risk are frequently in a monopoly position . . ."(39) Also, Sachs's restrictive fiscal and monetary policy would hinder not promote the development of domestic enterprises. The problem of entry is not satisfactorily dealt with by Sachs. Foreign competition and liberalizing regulations are insufficient and will not lead to the creation of capitalist markets in Eastern Europe.

III. MARKETIZATION: THROUGH PRIVATIZATION

Although Sachs urges the East European states to institute reform rapidly, change should be gradual because of complexity and the numerous links which imply that even if one element can be forwarded immediately its effectiveness would be hindered by the lack of other complementary factors. The Secretariat of the Economic Commission for Europe argues,

> There are some reforms which do not need to or cannot be put in place quite as quickly. These include: (1) creating an adequate regulatory environment, (2) starting the process of "large privatization" through the outright sale of state-owned enterprises, (3) creating some components of capital markets other than central and commercial banking . . .(40)

Sachs, however, uses the same reasoning to argue for rapid and comprehensive change. Because of the inherent complexity of the process of marketization, piece-meal or gradual change will worsen not improve the economic situation in Eastern Europe (the failure of the Hungarian gradualist strategy is used as evidence to support this position). Although a gradualist strategy is difficult and leaves room for many errors on the part of policy-makers, it is still indisputable that the lack of a capital market and a regulatory environment will negatively affect attempts generally to create a market.

This section will focus on the problem of privatization. How privatization evolves is of central importance because it is a main determinant of the future economic system--its structure and nature. It is privatization which most strongly indicates the difference between rapid and slower marketization approaches (and their outcomes). For example, rapidity (and therefore reliance on foreign capital) suggests that the future ownership structure would remain concentrated. Four dimensions of privatization that Stark develops are: "foreign versus domestic ownership; spontaneous privatization versus privatization controlled and directed by state agencies; institutional versus natural ownership; and concentrated versus dispersed ownership."(41) Also, privatization has two meanings. East European writers usually use privatization to refer to the process of transforming state-owned enterprises into privately-owned ventures. Privatization, however, can also refer to the development of the private sector (along side of the state sector) which does not necessarily imply radically transforming the state sector.

The benefits of foreign ownership typically raised are access to new technology and products; injections of needed capital; modern managerial skills; organizational modernization; and access to Western markets. In the case of East European states, the sale of state enterprises is viewed as one way to earn hard currency to reduce foreign debt. Foreign ownership, however, can be viewed as a moot point. The scale of foreign buyouts of state enterprises should not be exaggerated. Kornai writes, "I for one would not count on foreigners making a considerable investment in the Hungarian economy solely on the basis of the exceptional conditions offered them over Hungarian private firms [this is indeed the case]."(42) In 1989, in Hungary, the "average participation of foreign capital in the newly registered joint ventures is only twenty thousand dollars. A relatively small amount of capital is coming, mainly into the service sector [MacDonalds!]."(43) The relatively low foreign participation rate will not increase dramatically in the near future as unstable economic and political conditions in Eastern Europe make investment unattractive to Western capital.

One danger in promoting foreign ownership as a means to decrease the size of the state sector and to induce the formation of a market is the undervaluing and underselling of state assets. Undervaluing and underselling are not unlikely outcomes if speed in dismantling the state sector is the main objective.(44) (Which enterprises are likely to be purchased by foreign capital? Those firms that are already profitable.) One illustrative example was the General Electric purchase of a majority stake in Tunsgram, Hungary's largest lighting manufacturer, for US $150 million.(45)

> It was the biggest Western investment in Hungary since World War II, but GE did not exactly take a leap into the unkown: the joint venture teams GE with one of Hungary's most successful enterprises, an effectively privatized firm that already exports more than 80 percent of its products to the West. The deal also removes a GE competitor and improves the company's position in Europe and other regions.(46)

The current political bias directed against state-owned enterprises could easily lead to a situation in which Hungary has sold its top companies for ridiculously low prices and is left only with those enterprises already in trouble. Despite the claims that the state sector is horribly inefficient, it has, at least, been able to cover its own costs. In 1989 the state collected 238 billion forints from state enterprises while subsidies to state enterprises totalled only 235 billion forints.(47) If revenues from state enterprises collapse while the demand or need for subsidies remains relatively unchanged, then an already difficult fiscal position will worsen.

Another problem that Matolcsy raises is that "what is missing is the economic and social institutions that may act as checks on the privatization process."(48) Hungary lacks domestic capital, management expertise, developed capital markets, and a legal framework to act as a check on privatization. Moreover, there has been little time in Hungary for a serious discussion on the role and method of privatization.(49) Hungary created the State Property Agency (SPA) to manage privatization.(50) Its (contradictory?) functions include: a legal role (to supervise asset transfers); a bureaucratic role (to coordinate the process of privatization); and a commercial role ("to oversee the management of SOE's [state-owned enterprises] and to maximize state revenues as the ultimate owner of, or shareholder in, these firms.")(51) Although legal and regulatory institutions are important (and the SPA is likely to be insufficient in this regard), Csillag raises an important proviso: privatization is more than a legal issue and uniform rules are inadequate because of the diversity and complexity which characterize the state sector.(52) Instead, (rational) privatization will generally require a case by case approach.

There are two ways in which Hungary can privatize its state sector: "spontaneously" or through central (government) direction. An interesting but difficult problem has arisen because Hungary had "semi-privatization"--managers were given psuedo-ownership roles--in 1984.(53) Janos Martonyi, government commissioner for reprivatization in Hungary, argues "that the matter is much more complicated because, in fact, for the majority of enterprises, the state or government is unable to practise ownership rights."(54) This predicament has led to the unpopular practice of spontaneous privatization: the process of state managers themselves privatizing the enterprises which they operate. The abuses that can arise from this are evident; in particular, management has the ability to transform its political power into economic power by ensuring that the deal to sell includes an attractive package for itself. An argument for spontaneous privatization is that it must be allowed because of the scale of privatization that is needed. Centrally directed privatization is too slow, and it too can lead to abuse of power. There are several problems with this position, and Bod's response captures the most evident: "we cannot accept the position that after a system has for over fourty (sic) years ruined the economy and society, now this, a spontaneous cure, should take place so as to correspond to neoliberal tenets."(55) Impatience and the emphasis on rapidity may do more harm to the Hungarian economy than any other factors.

Another problem with spontaneous privatization is that "a multitude of private monopolies will arise in place of state monopolies."(56) There are no exact figures on spontaneous privatization but Martonyi estimates, that as of spring 1990, approximately 60 out of 1600 state enterprises had been spontaneously privatized.(57) On the one hand, this proportion may seem small; but, on the other hand, these (like most state enterprises) were very large with a total value of approximately 50 to 60 billion forints.(58) An emphasis on rapidity and spontaneous privatization suggests that concentration of ownership is likely to remain a problem. The East European monopoly problem (of a much greater scale than we see in the West) would not be eliminated. There are arguments which attempt to demonstrate that monopolies have beneficial qualities.(59) It is, however, difficult to apply these arguments to Eastern Europe which does not have functioning markets and where concentration of ownership has led to political bailouts and inefficiency rather than innovative behavior (as will be demonstrated, political bailouts quite possibly could continue if ownership of these massive units is simply transferred).(60) A rational approach to privatization would be gradualist and would entail greater control and direction from the center. Centrally directed privatization, in effect, would require the renationalization of much of the state sector. Because of the shift to multi-party elections, the center or government would also be viewed as the legitimate actor to supervise privatization. Economics and the need to maintain social and political consensus suggest that central direction is preferable to spontaneous privatization. Bod argues,

> Wherever I go in the country, eight questions in ten refer to the change in

> ownership. People are afraid that those who failed as politicians will appear as "parachutists" among the managers in new companies. We [the Hungarian Democratic Forum] also support privatization and even urge it. But it has to be seen that every process has some political feasibility. (61)

Related to domestic ownership is the question of whether institutional or natural owners should predominate. Stark summarizes,

> As for domestic ownership, rapid privatization would tend to yield patterns of institutional ownership of two broad types: 1) endowments of nonprofit institutions such as hospitals, educational institutions, and foundations; and 2) intercorporate holdings in which banks, insurance companies, and industrial enterprises hold shares in other Hungarian corporations.(62)

The first option is interesting, but it is arguably a longer-term strategy. What it implies is that a hospital, for instance, would hold shares in and receive its revenue from other Hungarian businesses. The hospital would have a definite interest in seeing that the businesses it held shares in were operated soundly and efficiently--that is, it would have a "real" ownership role. The central problem with this is that government decision makers will be tempted to use privatization as a means to reduce deficits and to cut endowments to non-profit organizations too quickly.(63) Given the current economic situation in Hungary, where should these non-profit organizations invest? If they find their endowments from the state radically reduced they may be forced to invest in riskier operations with a shorter-term pay off.(64) Furthermore, as Stark points out, the most rational strategy for non-profit organizations to follow may be to invest in only one corporation:

> But if almost any investment at this point in time is objectively risky, why not venture with a known and proximate entity? If the enterprise is in danger of failing, then all the better that the trustees of the endowment can walk arm in arm with representatives of enterprise management . . . Such are the basic ingredients for reproducing soft-budget constraints in the transition to a market economy.(65)

The second option of intercorporate holdings would likely accentuate the Hungarian monopoly problem as "cross-ownership and interlocking directorates will produce even more powerful mega-organizations."(66) Stark, however, emphasizes that the problem is not only monopolies, but also the lack of risk-taking in the centralized economies. The answer is to place state property "in the hands of natural owners--individuals or partners who risk losing their personal property if the venture fails."(67) Entrepreneurs are needed to bring about a competitive, efficient market. This solution is a longer term strategy that would require reregulation of the state sector and deregulation of the private sector. Initially the private sector would be fostered along side the state sector and would not immediately replace it. The state sector would be dismantled as domestic capital could absorb it. An argument for this strategy would be similar to the following sketched out by Stark:

> In Hungary, by contrast [to Western Europe], ninety percent of the economy's assets are state-owned, and habits and routines that have become second nature were shaped for four decades under the logic of soft-budget constraints. To transform the economy it is not enough to select new institutions; new habits must be cultivated as well. Because these cannot be created from above, we must start where they all ready manifested--in the existing second economy, where habits of risking one's shirt, of thrift and industriousness are commonplace.
>
> . . . And it is these clan networks [that characterized the old regime], combined with deeply ingrained habits shaped by soft-budget constraints, that cause us to fear that under conditions of institutional ownership firms will continue to look to the state for subsidies, and that their inordinate size will give them the means to blackmail the new state in the foreseeably long period of economic difficulties to

come.(68)

These fears are well-founded, but is this strategy based on romantic and idealized notions of the market and the entrepreneur? Briefly, the aim of this strategy is to promote the uninhibited develoment of small and medium sized firms whose ownership and management are directly linked, inducing risk-taking with real gains and losses. But can this be maintained? The dynamics of a capitalist market suggest that it cannot: arguably, concentration and centralization would evolve. The process of marketization and the market itself must be controlled to induce socially desirable outcomes--for instance, economic policy to limit the concentration of capital.(69)

The best known Hungarian proponent of dispersed (and natural) ownership is Ivan Szelenyi.(70) Szelenyi supports a policy that promotes the development of the private sector through deregulation; but does not argue for a rapid dismantling of the state sector and rejects arguments which urge a role for foreign capital. Szelenyi's strategy is long-term and would lead to a dual economy. Szelenyi argues,

> If the primary aim of economic policy is not to get rid as fast as possible of the public sector, but to deregulate, create new spaces outside the presently existing public sector, one may begin to think differently about what one expects from it.(71)

Szelenyi promotes a dual-economy because he recognizes the inherent difficulties of rapid, wide-scale privatization. Szelenyi emphasizes the need for a dynamic, entrepreneurial private sector, but also sees a role for the public sector.

However, one important question, posed by Stark, is will privatization lead to marketization?(72) Stark argues that we should not only consider the economy and its features, but also "social groups and the characteristics of their networks of affiliation that impede or facilitate marketization."(73) For example, it is important to consider the networks of affiliation that characterize the second economy. Stark argues,

> . . . state socialism prohibited the spread of the market in the past, but it also virtually eliminated any institutions of civil society that might form the basis for such cooperation in the near future. The networks of Hungary's small scale producers are so restrictive they provide little basis for cohesion and coordination. These networks are too close to the nuclear family, and their patterns of trade are too close either to large enterprises or to the

> final consumer (with relatively few purchase and supply links within the sector itself) . . . . In such an ecological model, entrepreneurship is less a function of individual motivation than of social relations in a particular field.(74)

This would indicate that the development of a market by deregulation may be insufficient or, at least, may take longer than is expected. Moreover, because of the close ties between the second and first economy (lack of intermediate connections), disruption and change in the first economy will negatively affect the heralded saviours in the second economy. This discussion also suggests that the impact of Sachs's transitional blueprint is not likely to be what he anticipates: the creation of a "market" and the process of privatization are not as simple and straightforward as he would indicate. Marketization will require more than stabilization and privatization. Stark concludes,

> If twenty years of experience with reforms demonstrated that markets are not possible without private ownership, the next decade of experience with transformation in Hungary might yet demonstrate that private ownership is not sufficient to create marketization. (75)

IV. CONCLUSION

What is the wisdom in believing that a version of Western-style capitalism, under hot-house conditions, can simply be recreated in Eastern Europe? Szelenyi, for example, criticizes Western economists for believing that entrepreneurs simply exist: "The neoclassical economist participating in the conference thought I was a fool; for him there was no problem. People behave rationally, so with the right rules in place they just will act in an entrepreneurial way."(76) Given the historically different circumstances in Eastern Europe, economically and politically, it is only sensible to conclude that its development will also be substantially different from that of the West. Sachs's policy proposal cannot be applied with the expectation that Western-marketization will result: the economy does not exist in a vacuum nor is it simply shaped as if non-economic factors were of no influence or importance. Sachs's policy will not create a market overnight nor will it lead to rapid integration into international markets or growth that promotes a higher standard of living for most of the peoples of Eastern

Europe. Rapid privatization would merely change the owners of East European capital--it would not dissolve the present blocks of concentrated ownership. Moreover, a restrictive macroeconomic policy would inhibit the development of a domestic bourgeoisie, suggesting that reliance on foreign capital would continue in the future. Szelenyi argues failure is inevitable if East European states choose a strategy "based on the massive import of multinational working capital."(77) It is very unlikely, Szelenyi continues, that the "Hungarians and Poles will [be able to] compete with the diligence and precision of the Taiwanese or Koreans in producing chips."(78) Do East Europeans desire to compete against the Koreans and what would they gain from such a strategy? In short, Eastern Europe should not be led down the path of another poorly conceived "economic revolution" (one "What is to be Done" proposal was enough).

CHAPTER TWO: MARKETING SOCIALISM

> [There is a] third alternative between the reforming Communists, who insist that the only way out of the current crisis is the rationalization of large firms, and the classical (nineteenth-century) liberals, who hope that Eastern Europe, by opening its windows to the fresh air of the market, thereby inviting massive imports of Western capital, can jump into Western Europe and become an equal partner of the countries of the European Common Market. The Third Way today means a radical break with Communist collectivism without transforming Eastern Europe into an outlet of West European or North American large firms.(1)

How will Eastern Europe "look" in five, ten, or even, twenty years? Two possible future scenarios are: (1) Eastern Europe as an "outlet" for Western firms; and, (2) the development of a dual economy which arguably could evolve into a market socialism not radically different from that developed by Alec Nove in The Economics of Feasible Socialism.(2) As outlined in Chapter One, Sachs's blueprint cannot induce an economic revolution that would bring East European states to equal terms with the West; instead, his strategy would further damage these economies while leaving them very vulnerable to external influences and disturbances. But, if privatization is promoted in a controlled and slow manner, and if marketization is not allowed to progress randomly and freely, then it may be premature to proclaim that socialism is dead. As Comisso argues:

> . . . even though virtually all new governments in Eastern Europe intend to reduce radically the size of assets in state hands, their practical ability to alter significantly the public/private balance in the economy rapidly through disinvestment is somewhat questionable. Ironically, market socialism could well become the solution by default in a major sector of the economy, political pronouncements to the contrary notwithstanding.(3)

The size of the state sector and the difficulties of massive disinvestment are not the only reasons for believing that we may see a stronger social democrat rather than classical liberal approach in Eastern Europe.(4) Environmental degradation characterizes all East European states, and clean-up and prevention require government intervention. Another example is the poor infrastructure which will require government action to rectify. Public goods will not be supplied by the market, and the need for and range of public goods in East European states indicate that an active state will be a necessity not an option.

Although many will point to the state as the source of these problems in the past, this does not change the fact that the state will now be needed to "clean up." Before considering criticisms directed against market socialism I will develop more fully the meaning of market socialism and why a market is necessary.

I. DEFINING MARKET SOCIALISM

> The issue that the left must address is how and to what extent the market mechanism can be used to achieve economic efficiency without creating the conditions for elitist capitalism to replace an antidemocratic command economy.(5)

> The aim, then, is a socialism that makes markets a tool of its nonmarket purposes. Socialists can argue, in liberating markets from the capitalist context which frustrates their virtues, the visible hand can use the invisible hand for its own purposes.(6)

Market socialism, generally speaking, is an economic structure dominated by public ownership, but it does not eliminate markets as means to allocate resources. Markets are viewed as necessary to induce economic efficiency through material incentives. Yet, the market also generates inequality and insecurity.(7) Market socialists hope to eliminate, through active state intervention and direction, the negative features of the capitalist market while using markets to encourage social, not only individualistic, ends. An important market socialist goal is to promote greater economic and political equality. Market socialism is different from a capitalist welfare state in that the latter does not attempt to control the market. Instead, a welfare state relies on social policy to eliminate some of the negative externalities which are inevitably generated by the functioning of a capitalist market.(8) A welfare state makes no attempt to limit or direct meaningfully the operation of the capitalist market, as it is ultimately believed that the pursuit of individual interests will maximize total social wealth.(9) Further, although a welfare state attempts to eliminate gross poverty and to improve the position of labour to capital to some extent, greater economic equality is not perceived as an important or even desirable end.(10) Market socialists view a welfare state as limited for both economic and political reasons. Economically, atomized decision-making leads to socially irrational, and often harmful, investment.(11) Politically, democracy is limited within a welfare state, argue market socialists, because political equality and democratic participation are impeded by extreme economic inequality.(12)

The structure for "feasible socialism" that Nove advocates is a dual economy with both a private and public sector. The "legally permissable" ownership forms that Nove would allow are:

1) state enterprises, centrally controlled and administered;
2) state-owned enterprises with full autonomy;
3) co-operative enterprises;
4) small-scale private enterprise, subject to clearly defined limits; and,
5) individuals.(13)

Social ownership of property would dominate Nove's version of market socialism, but private enterprise/property is not excluded. The immediate question that arises is what should be the size of the private sector--or what limits to private ownership does market socialism imply? Nove argues that limits must be clearly defined, but what limits? Typically number of employees is used as a guide to limit private ownership. This, like any limit, is arbitrary, but Comisso argues that concentration of capital limits are a superior and less arbitrary means to limit the size of the private sector.(14) Limited liability, for instance, would not be recognized beyond a certain point, leaving owners liable for debt once this limit is passed.(15) As private firms expand they would "turn to stateowned venture capital banks" for necessary capital, and the state-owned bank would "acquire equity in the enterprise itself."(16) Comisso views this as a way to limit the size/control of the private sector while not completely dampening incentives to expand and innovate. The size of the private sector, however, cannot be specifically pre-defined. Ferleger and Mandle perceptively argue, "If a private sector is both desirable and a potential threat, the critical question is not how much is permissable, but rather, who is to decide."(17)

Some problems that the market does create are inequality and concentration of capital. The degree of equality or inequality that a society is willing to allow is a political decision. How this political decision is made is the decisive question answering whether or not the given distribution is desirable. Ferleger and Mandle argue "The only realistic basis for limiting markets' negative impact is to politically empower (sic) precisely those most likely to be damaged by market functions."(18) Those who favour market socialism argue that the private sector, and the market generally, must be limited and controlled, and most would agree that these limits should be determined democratically. To realize their objectives, market socialists usually recognize that a change in attitudes or mores of a society is also necessary--that implementing market socialism is more than a technical, economic issue.(19)

Nove's feasible socialism blueprint includes both planning and the market as means to allocate resources: "an umlimited market mechanism would in due course destroy itself, and create intolerable social inequalities ["tolerable" inequalities would characterize this system], the state would have vital functions in determining income policies, levying taxes (and differential rents), intervening to restrain monopoly power, and generally setting the ground-rules and limits of a competitive market."(20) The state, in a market socialist society, would also play a central role in directing investment.(21) A structure similar to the one that Nove advocates is not unlikely to arise in Eastern Europe given the limits caused by the size of the state sector and the need for state intervention generally to promote a successful transformation. To promote transformation by relying on the uncontrolled development of the market would entail very negative economic, social and political consequences.(22)

Is market socialism viable? The defects of capitalism (gross inequality, the precarious position of workers and indeed of capitalist accumulation, negative externalities) are well-known; but can we eliminate these negative side effects and yet maintain desirable outcomes? Is this a Utopian vision in a bigger circle? Debates about socialist transition typically assume the existence of a capitalist market. Although questions about the roles of capital and labour markets may be similar, the absence of markets in Eastern Europe makes the promotion and development of market socialism a qualititatively different issue.

First we must develop more fully why the market is seen as necessary and why Eastern Europe must promote its development. Those who favour market socialism do not view central planning and socialism (public ownership) as synonymous.(23) Ownership and allocation may be related but are different structures. The market allocates resource and factor (labour, rent, capital) incomes. Market distribution of factor incomes is viewed as a major probl[illegible] economic agents are rewarded for luck or "merit", for example, not for need. If left to operate without interference, the market generates inequality and can lead to extreme poverty for a significant proportion of society's members. Market socialists do not want to eliminate the market (or inequality); but desire to control the market to produce socially determined goals--for example, the elimination of extreme inequality. The market is viewed as an instrument, not as a final arbiter.

Central planning and public ownership are not synonymous; but neither is a rigid market versus planning dichotomy a useful or accurate division. Auerbach, Desai and Shamsavari argue:

> But in the real world we observe not objective, anonymous economic "laws of the market", but a complex dialectical and symbiotic connection between firms, on the one hand, and the behavioural relations we reify with the name "markets" on the other.(24)

Auerbach, et al., are challenging Mandel's argument that as capitalism advances, markets are replaced by planning.(25) The argument that increasing concentration of capital leads to planning, eliminating the need for a market, suggests that socialism (as planning) can easily evolve out of capitalism. If the market, as a decision-making guide, is still used by capitalist firms and is not replaced by planning, then the imagined ease of the move to planning is questionable. Auerbach, et al., argue that capitalist firms use both planning and the market--that they are not opposites or alternatives, but that there exists a dialectical relationship between the two.(26) Moreover, technological revolution and concentration of capital do not imply that capitalist development is a simple uni-directional movement. One example that Auerbach, et al., use is the invention and initial development of the transistor by AT & T.(27) As they note, this is a classical example of the "Schumpeterian vision of the great monopoly" as "a key source of long-term planning and innovation."(28) The entry into the transistor market by small firms, however, turned the "semiconductor into a highly marketized commodity in a remarkably short period of time."(29) Auerbach, et al., summarize:

> Thus not only does marketization often emerge out of acts of planning, but the forms which planning takes in modern capitalist firms can only be understood in the context of the market existing "on the outside": this market environment has a crucial effect on the transformation of the internal structure of the firm and on its procedures for decision-making.(30)

Auerbach, et al., demonstrate that it is inaccurate to dichotomize planning and markets, and to argue that planning has simply replaced the market as a decision-making guide.

If planning and markets are not posed as opposites, then it is possible to recognize the fact that the use of one does not preclude the use of the other. What benefits, however, does the market entail that planning alone cannot achieve? Harrington argues that markets can play an important role in at least three areas: "the efficiency of the nonmarket sector, the relations between decentralized democratic enterprises, and consumer choice."(31) The market is seen as an important means to achieve efficient resource allocation and to improve productivity--or to induce "healthy" competition. Competition is not in itself a negative (capitalist) market phenomenon. Harrington argues, "there must be room in the new socialism for initiative from the base and one of the ways of encouraging that is precisely through markets that will reward . . . the most innovative producers."(32) Complete removal of financial incentives, if possible at all, is not a current option. A greater reliance on moral incentives requires a deeper change in social attitudes and this cannot occur rapidly or be enforced. The real problem for market socialism, presently, is to maintain the positive features of the market while eliminating its negative effects. For ease of discussion, markets can be broken down into three, more specific, categories: product, labour, and capital.

Regarding product markets, an important advantage over planning is consumer choice. A criticism of this position which immediately arises is that consumers are not sovereign: "the desires that markets respond to are very largely created by the market itself, and they are in that sense inauthentic."(33) A system, however, that shapes market outcomes through government planning and intervention is very different from a market that emphasizes only profit, not need. The negative effects of advertising (shaping consumer demand and waste of resources) theoretically can be largely eliminated under market socialism. Moreover, how can "consumer sovereignty" be assured through planning? Even if we reject Mandel's argument that markets have been (are being) replaced by planning, why is it not possible to introduce central planning as the primary method of resource allocation? Mandel argues:

> As the alternative despotism of wage labour, with its disruptive and destructive logic, imposes much graver hardships on much larger numbers, "majority despotism" certainly appears a lesser evil in the search for a just society than "minority despotism", including market despotism.(34)

Mandel argues that an "adequate average level of consumption" must be guaranteed to all individuals.(35) To accomplish this, planning is necessary because the market does not reward need. Mandel does not argue for "detailed" planning but for "central" planning.(36) "Industrial-social branches" would be given broad guidelines from above (indicative planning) and these broad guidelines would be determined democratically by a national congress.(37) How does Mandel overcome the problem of consumer choice? Mandel writes,

> Alternative demands on limited resources are neither ignored nor hidden. They are democratically settled at different levels. No rigid hierarchic structures arise from such institutions. This expressly guarantees producer/consumer sovereignty--i.e. selfdetermination, freedom in the real sense of the word--against both the tyranny of blind market forces and the tyranny of arrogant technocrats or bureaucrats.(38)

Consumers, for example, would be given a list of the different sorts of shoes that will be produced (in the coming production period), and then check which ones they desire.(39) This information is collected and passed on to appropriate departments for implementation. Even if this were technically feasible, it requires, as Harrington notes, "heroic consumers who would be willing to attend endless meetings in order to assure that they get exactly what they want."(40) Frankly, people arguably would prefer to use the market as the means to express their demand rather than to fill in numerous forms and attend countless meetings.

Finally, in regards to planning, is it viable? Dunn argues:

> In politics, as in war, as Clausewitz insisted, the crucial fact is that things never go according to plan. (It has proved to be an extremely important limitation of socialist economic planning that the amount of information required for rational choice at the centre of an economy can never in practice be secured there . . . . The massive advantages of the market mechanism from this point of view are the degree to which it economizes on information and the relative rapidity with which it responds to changes in expectation.) . . . it is indispensable for human organizations to be well adapted to whatever degree of partial ignorance of the conditions in which they have to operate is ineliminable.(41)

Dunn's reference to Clausewitz is useful becase On War indicates very clearly that "friction" limits our capacity to plan, and that the ability to overcome the consequences of plans gone awry is what leads to success.(42) Moreover, Clausewitz argued that war is not merely a technical phenomenon, it is also a human one; hence the human element must be included in a theory of war.(43) The human element includes the effects of limited knowledge, and moral and psychological forces.(44) Economics is also more than a technical, administrative phenomenon and economic theory too must include the human element. Because of the inherent human element (limited knowledge/information and moral and psychological forces), planning cannot solve all economic dilemmas and the market can play a useful role in limiting these difficulties. What if the plan cannot account for and satisfy every need? Why should it be illegal for individuals (within a market) to fill the gaps, or satisfy the demands, that planning cannot? If a legalized market is not allowed, the human element suggests that a black market would arise to satisfy demand. A market would most likely develop in the consumer goods and service sectors; but it would not necessarily be limited to these sectors. Although a transportation infrastructure, railroads for example, is typically perceived as a monopoly good, there is sometimes room for private enterprise to improve the efficiency and quality of transportation.(45) Why not allow a market to operate (within defined limits) to improve economic performance and to meet demand, when it is clear that a central plan cannot cover (adequately and/or competently) every contingency?

A market cannot be used, argues Mandel, because its negative effects cannot be neutralized.(46) But why does satisfaction of basic needs imply that the market must be abandoned--that only central planning can achieve this? Can redistribution ensure that basic needs (as defined by society) are met? Miller and Estrin argue that "It is quite feasible to think of a division of social resources between those earmarked to satisfy needs and those serving to reward merit, and to provide the incentives that are required to make a market sector function effectively."(47) If markets, per se, are not defined as inherently "bad", then Miller and Estrin have raised the fundamental question about market socialism: can we intervene or control market outcomes, yet maintain a market that functions effectively? The two problem areas are labour and capital markets, not product markets. If basic needs for all people are met or guaranteed by political intervention, then the use of the market to allocate products to consumers is a moot point. In fact, it is arguably preferable to planning because it is easier for consumers to practise freedom of choice and it is more likely to dissolve bureaucratic power and control than planning (despite Mandel's assurances).

How do we control labour and capital markets, however, without eliminating their positive as well as negative outcomes? Miller and Estrin write, "market socialists want to have a free market in products, and either no market at all, or a well-regulated market in labour and capital."(48) Harrington argues that "the plan decommodifies the labor market and treats workers as human beings but it does so in response to signals from that labor market."(49) The example that Harrington develops is that of the Swedish labour market.(50) Harrington recognizes that the Swedish model cannot be simply transposed to other societies and that it does not eliminate many of the problems and tensions of, for instance, class conflict; yet, it does demonstrate that planning and the market can both be used to ensure "efficiency" and to protect labour from the dislocative effects of the market's operation. This approach would require that unemployment is viewed, politically and socially, as unacceptable--that full-employment, not the reduction of inflation, for example, is a social priority. Inflation would not be ignored; but neither would policies to control inflation entail injurious side-effects on employment. Further, control of the labour market does not imply that plant closures are avoided, or guarantees for the same job are made. The Swedish model "proceeded to change the consequences of that market outcome by selective measures that saw to it that the worker would not suffer as a result of shutdowns or rationalization."(51) Harrington argues that it is not the labour market that is injurious: it is the "social conditions" that effect the operation of the market and determine the conditions under which the wage bargain is made.(52) The wage bargain, under capitalism, is determined by the unequal position of labour to capital:

> So labor markets under capitalism, based on economic rather than political coercion, forced workers to "freely" sell their labor power at a fair value that produced more for the capitalist than it cost.(53)

If labour is not economically coerced into selling its labour power (because basic needs are guaranteed), then conditions under which the wage bargain is made would change, and, in turn, "market outcomes would be different."(54)

Although changing the conditions under which the wage bargain is made does not eliminate all problems, it is a feasible solution that improves the position of workers. Managing the labour market is largely a political rather than a strictly "economic" problem.(55) The real "economic" difficulty for market socialism lies in the control and operation of the capital market. Decentralization and a private sector, regardless of size, necessitate a capital market. Control of investment, however, is also a central tenet of market socialism. Nove writes,

> Investments would be divided into two parts: those of structural significance, usually involving either the creation of new productive units or the very substantial expansion of existing ones, and those which represent an adjustment to changing demand (or to new techniques). The latter would be the responsibility of management (cleared as required with the elected committee), and the necessary finance would be obtained either from retained profits (and reserves based upon past profits) or from credits from the state banking system.(56)

Market socialists desire to control investment decisions to ensure that future outcomes are compatible with social goals, yet view the market as playing a key role in calculating and determining investment decisions. Markets, as Auerbach et al. point out, "offer a framework in which planning for the future can start from 'actually existing' demand and cost parameters, and not merely from abstract, conjectured notions about what is 'needed' by society and about what is an 'adequate' level of efficiency."(57)

Comisso argues that "providing for a capital market and for the entrance of new competitors are critical for a socialist economy to function."(58) Further, she writes, "My own personal belief here is that the fundamental obstacle to the creation of self-regulating markets in socialism is precisely the lack of provisions for entry into the socialist marketplace."(59) Without adequate provisions for entry it will be difficult to enforce hard budget constraints, and entry and exit imply the existence of or need for a capital market. A market socialist economy must allow failure and promote entry; but how is this to be accomplished? Miller and Estrin write:

> Take capital first, and consider decisions to invest in this or that productive enterprise. Such decisions are of their nature harder to make than (typical) decisions about consumer goods; to be rational they need to be based on complex judgements about the future performance of enterprises. . . . it is misleading to pretend that capital poses no special problems for the theory of markets.(60)

How do we allocate publicly-owned capital prudently? Who should determine the lending rules, and what should they be? If a central bank is given power to direct investment should it follow, for instance, an investment returns criterion? One possible problem with this is that enterprises would be motivated to run down assets to boost the technical rate of return.(61) A formula for sagacious and farsighted capital investment has not yet been discovered. Although there are no easy or obvious solutions to controlling investment or operating (successfully) a capital market, neither has capitalism solved these dilemmas.(62)

II. CRITICISMS OF MARKET SOCIALISM

An important criticism directed against market socialism is the supposed incompatibility of public ownership and the market. For the market to be effective, it is commonly assumed, private ownership must predominate. Socialism failed because of the "impersonalization of ownership: state property belonged to everyone, and so to no one."(63) Comisso agrees that the impersonalization of property leads to serious problems, but she also argues that "state, social, cooperative, and private ownership are all alternatives to the previous system [the centralized model], and none can be summarily dismissed as a priori 'inefficient' on the basis of previous experience."(64) Comisso takes this position for two reasons: she stresses the need to demarcate clearly the boundary between the proprietary (economic) and communal (political) spheres--the centralized economies did not do this; and, argues that the "problem in 'actually existing socialism' was communal ownership, not 'state' or 'social' ownership in and of themselves."(65) Comisso argues:

> Because laws in general were subordinated to political priorities, property rights defined in laws necessarily suffered the same fate, regardless of who held them. As a result, the "norms of behavior with respect to things" in practise corresponded neither to the state, "social"/self-managed, cooperative, or private ownership system but rather came to resemble the communal ownership arrangement.(66)

Comisso argues that property rights are essentially legal rights which introduce a separation between proprietary and communal spaces.(67) The political dominance of one party in East European states led to a lack of distinction between economic and political spaces: "As a consequence of the role [of the party], even the state lacked clear title to its assets, as party officials could and often had to intervene in the actions it took to dispose of them."(68) The centralized economies lacked genuine economic agents because of the monohierarchical nature of that system. Comisso argues that property rights must be controlled by economic actors and that economic and political spaces must be kept distinct for a market to work.(69) This argument is different from those that merely stress the need for private property because, as Comisso points out, her argument does not imply unrestricted property rights, nor does it claim that economic actors must be (private) individuals.(70) Economic actors could be state or publicly-owned enterprises.

A lack of genuine economic actors implies that ownership is communal not public. Property rights "serve to define the feasible set of exchanges within a given economic system . . . [they include] the right to use, to derive income from the use of, to exclude others from, and the right to exchange the goods (or services) in one's possession."(71) Communal property does not specify or entail these rights and/or these limits to use: it is characterized by the principle of nonexclusion.(72) Communal property relations lead to problems because it is difficult to eliminate externalities--individual users have no interest, for instance, in preventing waste or overexploitation of resources.(73) Comisso compares the effects of communal ownership with those Kornai elucidates in regards to the soft-budget constraint: "producers are relatively insensitive to costs and thus [are] open to pursuing goals justified on political grounds. The result was that those who could affect the income flow deriving from the state or society's assets do not bear the economic costs (or benefits, for that matter) of their actions."(74)

To prevent the development of communal property relations, Comisso suggests that a neutral third party is necessary "to adjudicate disputes arising out of transactions between economic actors with legally specified property rights, typically an independent judiciary."(75) Comisso envisages "property rights as a system of public rules" that political authorities would establish, and an independent judiciary would enforce.(76) The determination of property rights would be a collective/political act and these rights could be modified to reflect changing circumstances.(77) Comisso, however, stresses that "if the same institution that exercises property rights also specifies them, modifications will reflect the immediate exigencies of the possessor, rather than their general effects."(78) For this reason, political and economic actors must be distinct; but this structure would also link genuine political authority and genuine economic actors together.

Comisso challenges the assumption that private ownership is necessary for a market to work effectively: "While there is a great deal of empirical evidence supporting this proposition, its theoretical status remains contested . . ."(79) Comisso uses the example of publicly-owned firms, subjected to market conditions, which have not had inferior performance compared to privately-owned firms.(80) Comisso presents an argument and structure for market socialism:

> . . . if ownership rights are lodged in the hands of public [economic] actors within a regulatory and incentive structure that guarantees that their decisions reflect a genuinely economic motivation, a real test of the feasibility of "market socialism" would finally become possible.(81)

The difficulty or tension in market socialism would be promoting "genuine" economic motivation. Genuine is difficult to define but it suggests that economic categories such as profit and efficiency would determine economic behavior. Yet, market socialism, by its very nature, implies that economics is politicized--that the purpose of the market is to promote political and social ends, not economic. Despite this tension, which may be impossible to resolve in a market socialist system, Comisso is correct generally in pointing to the problems generated by communal ownership and for the need to maintain a distinction between political and economic actors.(82)

Another important criticism of market socialism often raised is that Hungary attempted to institute market socialism with the NEM and its failure proves that market socialism is unviable.(83) The NEM of 1968 cannot be described as an overwhelming success and, except for the immediate five years following the introduction of the NEM, economic performance in Hungary can be categorized as dismal. The NEM was plagued by retreats and inconsistencies that make it difficult to determine if alternative results would have been possible given the same goal (an attempt to create market socialism). The political effects on economic reform, however, must be emphasized: in particular, the continued centralization of political power and its clash with attempts to decentralize the economy. As Comisso and Marer stress "when reform measures seemed to impede central control of the economy and jeopardize the attainment of central policy objectives they were expected to facilitate, the NEM began to be reversed . . ."(84) Or, as Szamuely argues, "The reform [NEM] did not intend to touch the system of economic and political institutions, i.e. the power structure of society, whereas it did intend to change somewhat the way of exercising power."(85) These limited intentions for reform meant that it "could not reach beyond establishing a centralized indirect system of control and management."(86)

Although the Hungarian Socialist Workers' Party (MSzMP) differed significantly from other Communist parties in Eastern Europe (in particular, the active role of reformists in the MSzMP), power was still centralized and the MSzMP maintained firm control over state apparatuses and mass organizations (trade unions, youth organizations, etc.).(87) Moreover, even though reformists were active in the MSzMP, their commitment to the party and Hungary's political structure made them "politically weak and obstruct[ed] consistent implementation of their policy preferences."(88) Pressures for change had to be balanced with the maintenance of party power and control. The supremacy of the MSzMP also led to what can be described as perverse actions by the leaders of the party and of mass organizations:

> The centralized state, the "transmission belt" mass organizations [with party appointed officials], and the hierarchic distribution of power in the party all place a premium on having influence in the center and provide disincentives for leaders to exercise power unilaterally for their own goals.(89)

Because power remained centralized, regional party leaders, for example, were not supportive of private agriculture despite its local popularity: "supervision of big industrial complexes of national importance is what counts politically", not popular support.(90) This focus on the center also permeated mass organizations with the same result: it was not membership support that counted but size and strategic value.(91) Further, given the Hungarian political structure, popularity from below was not an important or desirable asset. It was those above who determined and rated an individual's qualifications and promotions.

Kadar introduced the principle of collective leadership in 1956. The purpose of this was to prevent domination by a single leader (Stalinism) and more generally to act as a check on the power of top leaders. The four elements of collective leadership in Hungary were:

1) the socialization of political power;
2) tolerance of diversity within the party;
3) restrictions on political resources; and,
4) decision making by consensus.(92)

Collective leadership magnified the tendencies which promoted MSzMP dominance. Political power, within this structure, derived from the "ability to influence collective decisions" of the party, not from the "successful" operation of the organization that the individual represented (enterprise, trade union, etc.).(93) Further, since all derived their power from the same source, it was in no one's interest to weaken the influence of the party. Thus, although tolerance for diversity was allowed, consensus and cooperation were the norms not disruption or direct confrontation. Restrictions on political resources referred to the limits placed on individuals in developing support below or outside of the party. Again, this threatened the power of the party and, in turn, its members; hence there was little motivation for individuals to build external support at any rate. Or, as Comisso and Marer point out, "Exercising influence thus gives leaders an incentive to reduce the relevant public; in effect, the very conditions that preserve limited pluralism in the party work to prevent the emergence of real pluralism in society."(94)

The effects of economic reform and the political structure of Hungary led to several contradictions. The first, as was noted, was the tension between economic decentralization and attempts to maintain political centralization and control. Of great importance was the weak support of regional elites for reform.(95) Because power continued to mean power in the center, the break up of state enterprises within the regions negatively influenced regional power. The political incentives for big state enterprises were inconsistent with the general economic interest for smaller state enterprises. Another unexpected result for reformers was that reform strengthened the non-state sector; although its intent was to strengthen the party, or more importantly the sector that the party controlled: the state sector.(96) Hungarian experience indicates that a decentralized political system is a necessary (though not sufficient) requirement for successful economic reform. Hungary had its first free parliamentary elections in the spring of 1990, eliminating past political structural limits. How this opportunity will be used, however, is another question.

III. CONCLUSION

Public or state ownership of property is likely to remain the domimant form of property relation in Eastern Europe for some time. The limits due to the size of the state sector and the wide need for public goods suggest a continuing role for the state. Rapid disinvestment in Hungary is proving unsuccessful. Michael Meyer (sadly) notes: "The [Hungarian] government's massively hyped sell-off of state-owned industry has fizzled disastrously."(97) Moreover, marketization plus a social policy will prove insufficient given the scale and scope of the transformation. An active, state-directed industrial policy will also be needed to restructure, for example, the large steel industry in Eastern Europe.(98) As Milenkovich notes, "Coming to terms with a decaying steel industry has been enormously costly even in well-functioning market economies, such as the United States and France."(99) There may be disagreement on how well-functioning these economies are, but adjustment to a rapidly changing global economy has proven difficult for all states.

A gradualist strategy would cause the current generation of East Europeans less pain, and could, in the future, lead to market socialism. Market socialism is a preferable and viable long run alternative. Market socialism, unlike capitalism, does not give the atomistic firm total authority. Limits on the market and private ownership are used to promote socially optimal outcomes (for instance, to prevent negative externalities). Economic information in a market socialist system would primarily be generated and transmitted through a market or prices. Central planning (characterized by vertical relations and "quantified" information) is limited in its ability or capacity to plan rationally and prudently. The market is necessary for reducing the difficulties associated with limited knowledge, and as a means to reward (and punish) economic behavior. The coordinating mechanism of market socialism is a hybrid of markets and planning--they are not viewed as mutually exclusive. Instead, the primary question concerns the weight each should be given.

CHAPTER THREE: POSSIBILITIES AND LIMITS

> The political analogue of the socialist hope that culture can in the end dominate structure and human values govern the organization of production is the hope that this dominance can be secured through the construction and sustaining of a political culture of mutual credibility and goodwill. The charade of belief can be mustered by any capably repressive political order. But the actuality of belief has to be fought for and won incessantly.(1)

Promoting the development of market socialism is more than an economic, technical or administrative problem.(2) Changes in economic structures are not sufficient in creating market socialism (or, as this essay has argued, capitalism) because an external economic structure is not the only factor which affects human behavior. There are economic reasons for believing market socialism is a possibility in Hungary, but what are the political, social, and cultural characteristics which can also support this proposition? This chapter will consider social and political possibilities and limits to promoting market socialism in Hungary.

I. POLITICAL POSSIBILITIES

The Hungarian Roundtable negotiations, which started 1989 June 13, led to free elections and a parliamentary political system within a year. Bruzst and Stark note that "Unlike the strong presidencies that have highjacked transitions from authoritarianism elsewhere in the world, Hungary now has a governmental structure with a weak presidency and a strong Parliament."(3) The different political structures which evolved, for example, in Hungary and Poland were due primarily to differences in the strength and nature of the political oppositions: respectively, a weak and strong opposition. The opposition movement in Poland--Solidarity--was viewed as a legitimate voice for the Polish people by the Polish people.(4) In Hungary, as Bruszt and Stark write, the opposition "With their organizational membership still numbering only in the thousands, and with their strength in society still untested, they could neither make an undisputed claim to speak in the name of society nor anticipate the capacity to call on society to agree to a compromise."(5) The principle that unified the Hungarian opposition at the Roundtable negotiations was the need to hold free elections to legitimize political power.(6) The Opposition Round Table (EKA) argued,

> There is no legitimate power in Hungary today. Until legitimate authority is created through fully contested free elections, no organization--including those in the opposition--has the right to decide the nation's future political and economic institutions.(7)

Generally Hungarian Communists also supported free and uncontested elections because they believed that it was possible to gain enough electoral support to maintain political power.(8) Public opinion surveys published in May 1989 indicated that,

> . . . if elections were to be held immediately, the communists would win a decisive plurality of the votes . . . . The surveys also indicated that the opposition parties would be hard pressed to field candidates for national office. A majority of respondents did not recognize the names of the opposition's leaders, whereas Pozsgay, Nemeth and others [Communist leaders] were not only widely recognized, but also growing in popularity.(9)

Given the general uncertainty in Hungary and the lack of any one strong political group, all political groups saw it as potentially beneficial to allow free elections.

One area of initial disagreement between the EKA and the Communists was over the role and powers of the President and the Presidential office.(10) Hungary, unlike Poland, did not have strong, recognizable opposition leaders. Indeed, as the above quote emphasizes, individual Hungarian Communist leaders were popular at this time. The first agreement, signed 1989 September 18, would have created a strong Parliament and allowed the office of President to be elected directly, with the first elections to be held in November 1989.(11) Early and direct presidental elections benefited the Communists since their leaders enjoyed popular support and a quick election would have prevented the opposition from gaining much force or momentum. This first agreement, however, was challenged by FIDESZ and SZDSZ who portrayed it as a "deal" which failed to threaten seriously Communist power.(12) FIDESZ and SZDSZ were able to force a referendum on the presidential clause, which they narrowly won.(13)

Because of the delay caused by the referendum, elections were not held until the spring of 1990. During this time the opposition took full advantage of anti-

Communist rhetoric. Although economic crisis characterized Hungary, it was not a prominent issue during the 1990 election. Instead, the first free parliamentary election in Hungary was dominated by anti-Communist rhetoric.(14) Anticommunism and the lack of economic debate were not unrelated features. As Comisso points out, "Since class-based appeals were, literally, out of order, the basic economic issues invariably raised by conflicting class interests never became politically central."(15) "Class-based appeals" connoted "Communism", and hence were avoided.

Politically, uncertainty and a weak opposition in Hungary led to a relatively strong consensus for the need to have free and open elections. The political transition from a one-party state to a competitive party system occured relatively rapidly and painlessly in Hungary: hence, the "silent" revolution. Bruszt and Stark argue, "With only a few exceptions, the new political elite in Hungary is one with a high degree of agreement about the formal and informal rules of the game."(16) Hungary has established an open, decentralized, competitive political system, a necessary condition for economic decentralization and reform. Institutionally, the political framework established in Hungary in 1989-1990 is not incompatible with market socialism, nor is the problem a lack of political debate on an alternative development model. Currently in Hungary, as will be developed, major obstacles to market socialism, and greater reform generally, are the weak ties between civil society and Hungary's new political parties, and political apathy (lack of "public" debate).

II. POLITICAL PARTIES IN HUNGARY

Politics in Hungary can best be described as fluid and, as Kovacs notes, attempts to discuss Hungary's future are "a sort of intellectual masochism."(17) Yet, a brief sketch does demonstrate that a Western-style market is not as widely desired as rhetoric in the West would indicate. The predominant values and ideas of the various Hungarian political parties suggest that "social democratic" rather than "classical liberal" best describe Hungarian political attitudes.

The first free Hungarian elections, held in the spring of 1990, led to a coalition government comprised of the Hungarian Democratic Forum (MDF), the Christian Democratic People's Party (KDNP), and the Independent Smallholders' Party (FKGP). The opposition is dominated by Free Democrats (SZDSZ) and the Young Democrats Alliance (FIDESZ). The Hungarian Socialist Workers' Party (MSzMP) split in 1989 with the "orthodox" Communists establishing a new party with the same name, and the "reformers" creating the Hungarian Socialist Party (MSZP). These two parties were soundly defeated in the election with the MSZP receiving about ten percent of the vote.(18) The defeat of the "left" in Hungary can largely be explained by the general negative feelings or even hostility towards the old Communist parties, rather than a radical shift in the ideological orientation of Hungarians. Laki notes,

> No doubt, the majority voted for dirigist programs but, at the same time, liberal economic thinking also has strong support in Hungary. More interesting is that a lot of people refused leftist-dirigist programs and voted for centrist (conservative)-dirigist programs. In other words, the non-economic distinction between left and right proved more important than the economic philosophies of the parties.(19)

The first election in Hungary can be characterized as a negative--"no to Communism"--vote.

Andras Bozoki breaks down Hungarian political trends, shown in the following table, giving an overview of the ideological orientation of the many Hungarian parties.(20)

TABLE ONE: Political trends in Hungary.

TRENDS	LEFTIST CONSERVATIVES	CONFORMIST TECHNOCRATS PRAGMATISTS	DEMOCRATIC SOCIALISTS, REFORM COMMUNISTS	RADICAL-LIBERALS
VALUES	Bolshevik-Stalinist	value-neutral	Socialist democracy	Welfare state
ISSUES	one-party system	democratic centralism	limited multiparty system	multi-party system
	order vs anarchy	party unity	socialization of institutions	representative democracy
	COMECON autarchy	power maintenance	local self-government	social policy
	centralized planned economy	stability	socialist mixed econ	mixed econ
	cells in the structure of employment	----	"ideal" (non-statist) socialism	----
ORGANIZATIONS	MSzMP	Hungarian Socialist Party (MSzMP)	MSZP	SZDSZ
	----	----	Union for Leftist	FIDESZ

TABLE ONE: Political trends in Hungary, continued

	----	----	Alternative (BAL)	Hungarian October Party (MOP)
			Democratic Youth Alliance (DEMISZ)	
			----	Independent Smallholders' Party (FKGP)
SOCIAL BASES	older party apparatchiks	bureaucracy	younger generation MSZMP	urban middle class
	----	some former MSzMP members	intellectuals	working strata

TRENDS CONT.	SOCIAL DEMOCRATS	DEMOCRATIC POPULISTS	POPULIST CONSERVATIVES
VALUES	civil liberties	"Third-Way"	National identity
ISSUES	multiparty system	multiparty system	romantic concept of nation and community
	representative democracy	self-governments	society as a moral phenomenon
	social minorities	direct democracy	collective rights
	human rights	Hungarian minorities	Hungarian minorities

TABLE ONE: Political trends in Hungary, continued

ISSUES	social policy		traditions
	mixed econ	mixed econ	organic improvement
	free ventures	local communities (Garden Hungary)	"God-Family-Nation"
ORGANIZATIONS	Young Social Democrats (SZIM)	MDF	MDF-right wing
	Hungarian Social Democratic Party (MSZDP)	Hungarian People's Party (MNP)	Party for Independence (MFP)
	FIDESZ-SZDSZ left-wing	------	Christian Democratic People's Party (KDNP)
SOCIAL BASES	urban intellectuals	countryside intellectuals	non-urban
	students	middle class	----
	private entrepreneurs	private entrepreneurs	

SOURCE: Andras Bozoki, 1990.

The first impression that this table leaves is that it is difficult to distinguish between the various Hungarian political parties. Economically, the "radical-liberal" group (the extreme right in Hungary) advocates a welfare state. The "left" does not have a future in Hungarian politics. The policies of the leftist conservatives are anachronistic, while the reform communists are tainted simply by their past association. The "value-neutral" technocrats are currently limited as a political power; but their positions and training leave them in an advantageous position to gain from economic reform.(21) The other political parties generally appear to have similar programs and concerns. Bozoki attempts to separate political trends using a "Western" left to right economic-political spectrum. Such a spectrum, however, may not be the best way to attempt to visualize political differences in Eastern Europe or Hungary. Comisso writes,

> In contrast [to a Western political spectrum], the post-socialist political spectrum is structured along gemeinschaft-gesellschaft lines, with parties proclaiming a return to traditional, national communitarian values facing off against parties proposing more individualistic and Western models of development.(22)

Western conceptions of what it means to be a "liberal", for instance, do not work well in delineating Hungarian political parties.

One reason for the blurred distinction between Hungarian political parties is in fact the similarities in their economic policies. Laki argues,

> The programs of the new independent organisations are, in many respects, similar to one another. They draw primarily on the concepts of Hungarian radical reformers in the 1980s . . . . Almost all opposition organisations draw heavily on the traditions of Keynes, or more concretely, on those of Social Democratic ideas.(23)

All the parties listed above see a central role for the state in providing and developing infrastructures (including educational and cultural), and in promoting research and development.(24) Further, environmental protection has become a prominent issue in Hungary and cleanup necessitates state action.(25) Political party attitudes in Hungary toward state intervention are ambiguous, even contradictory. Laki, for instance, writes "The distrust of the healing effects of the market has even pentrated the consciously liberal program of the Free Democrats' [SZDSZ] 'Program for Changing the Political System.'"(26) The MDF, in fact, promotes a gradualist, nationally-oriented development policy ("Garden Hungary"), and rejects a liberal international integration strategy. Laki refers to this general market skepticism in Hungary as the "Survival of planning illusions--[or] instinctive distrust of the market."(27)

The current Hungarian coalition government, using Bozoki's framework, is a mix of Democratic Populists, Populist Conservatives, and Radical-Liberals. The attitude of these three governing parties (MDF, KDNP, and FKGP) towards privatization is not hostile; but neither do they promote "rapid" privatization. The MDF and KDNP both share the view that "Privatization should only be implemented in a careful, deliberate manner, in areas where it will benefit the whole economy."(28) The FKGP favours the privatization of land and it is the only party to argue seriously for restoration and restitution of private property.(29) The Young Democrats (FIDESZ) and Free Democrats (SZDSZ) are the strongest proponents of rapid privatization, yet they recognize that "capital from both Hungarian private persons and foreign investors could purchase only twenty to thirty percent of the state-owned companies' assets over the next few years."(30) Most political parties in Hungary seem to favour slower privatization--even if for practical rather than ideological reasons.

One important difference between the various parties in Hungary concerns "who" should be the primary owners of property. Both the MDF and KDNP favour employee ownership (purchase of stock by workers)--or, dispersed ownership patterns.(31) SZDSZ and FIDESZ promote greater institutional ownership, primarily because this is a more rapid way to privatize.(32) All parties in Hungary have raised concerns about underselling state-owned assets to foreign capital.(33) Direct foreign investment, not the sale of state-owned enterprises, seems to be the preferred policy option. As was discussed, government control and direction of privatization will require renationalization, and gradualism will be necessary to avoid foreign capital domination. How Hungary's privatization policy will evolve is yet to be seen.

Interestingly, it is SZDSZ and FIDESZ who argue that a wide social safety net is needed.(34) Laki argues that two kinds of welfare policies are advocated in Hungary because there are two different attitudes regarding the future: optimistic and pessimistic.(35) The optimistic groups include the "centrist" parties (MDF, KDNP, KFGP), and they do not see social aid as a primary issue because they believe that the economic crisis will be relatively short-lived, while SZDSZ and FIDESZ believe that the crisis is much deeper and requires more radical, immediate reform (which would entail greater reliance on the market, not the state) than that proposed by the centrist parties.(36) The centrist parties do not view a wide social-welfare program as necessary because their strategy is gradualist and will induce, they believe, "small" social costs. Unfortunately, even a gradualist strategy will probably involve more than minimal social costs, and the current social safety net in Hungary is likely to be inadequate.(37)

The "Democratic Populists" (or the "Third Way" trend) do not consider themselves to be market socialists.(38) The Democratic Populists reject planning, capitalism, and reliance on foreign capital. Domestic accumulation, through policies that favour and encourage the development of Hungarian-owned small and medium sized firms, is the third-way priority. Further, they do not reject a role for the state or public sector. Despite the refusal to declare themselves "market socialists", the left wing of the Democratic Populists, in particular, advocates an economic structure not radically different from that outlined in

Chapter Two.(39) This refusal to be thought of as market "socialists" is largely related to the negative feelings that the term or word socialism activates. It is somewhat superficial, however, to view this as strictly semantics. Kornai, for instance, supports a controlled marketization process and recognizes the need to promote Hungarian embourgeoisement.(40) Yet, Kornai does not view this as market socialism and firmly believes that market socialism would fail if attempted.(41) Many, like Kornai, believe that market socialism had been given a chance in Hungary, it proved unviable, and now a more "liberal-oriented" marketization strategy is required.(42) Although the past failure of economic reform in Hungary has led to skepticism about "market socialism", it has not led to an unthinking acceptance of capitalism or to the type of strategy outlined by Sachs. The "Third-Wayers" in Hungary have placed an alternative development model, with a domestic rather than international focus, on the political agenda and they are not an insignificant Hungarian political force.

It is unlikely that a rapid strategy--as was attempted in Poland--will be promoted in Hungary. Such a turn is unlikely, even if the MDF loses power and is replaced by "radical-liberals".

> Twenty-four percent of Hungary's eligible voters would not turn up at the polls "were there to be a general election next Sunday," the Hungarian Gallup Institute found in the latest of the month party preference polls it has been conducting since May [1991]. A futher 19% of the 1,500 adult Hungarians asked by Gallup could not single out a political party as their favorite. Gallup, quoted in the daily Nepszabadsag, said these figures have been practically the same throughout the past five months.
>
> As far as potential voters are concerned, the majority (33%) would support the opposition Alliance of Young Democrats (FIDESZ), which received only five percent of the votes in the country's first post-communist democratic elections in April 1990. The likewise opposition Alliance of Free Democrats (SZDSZ) would tie, according to Gallup, with governing coalition-leader Hungarian Democratic Forum (MDF) with 18% each. In 1990, the MDF won the elections with 42%, while SZDSZ received 24%.(43)

The growing popularity of FIDESZ does not indicate that rapid "liberalization" is necessarily around the corner in Hungary. FIDESZ does not support a classical liberal approach, but is more accurately portrayed as a welfare state advocate. The following quote taken from a FIDESZ political pamphlet supports this classification:

> However, a market economy does not ensure citizens' equality of opportunity, it

> produces and reproduces inequalities. The political institutions of democracy are not capable in themselves of healing inequalities that so arise. For this reason, a conscious social policy is needed to set aright the social disadvantages that develop and to create equality of opportunity. However, this social policy cannot mean the elimination of the market economy, nor should it produce a centralized economy that leads to the elimination of democracy.(44)

A capitalist welfare state is not market socialism, but the promotion and development of either one will take time.(45) During the transition, if FIDESZ attains political power, it may find that it has to take an active role in directing the economy. Reliance on a social policy will prove insufficient given the major industrial restructuring that is also required. Hungary, like other East European states, needs a far-reaching industrial policy. To date, this is where the problem lies. An important obstacle to reform in Hungary is lack of policy--not a radical neo-liberal agenda nor a rigid rejection of a role for the state.

III. POLITICAL AND SOCIAL LIMITS

Deborah Milenkovich writes,

> One component missing from the process of

> transition in East Central Europe is becoming increasingly clear: There is no industrial policy in any of these countries. It is unclear whether this is because of a belief in the sufficiency of the monetarist prescription of stable currency and competition, a profound revulsion at the idea that the state must continue to play an important role in the economy or a shying away from the truly difficult task of closing down major sectors of the economy.(46)

Bruszt and Stark write,

> To date, these [economic] policies have not been particularly innovative, coherent or consistent. The most striking aspect of the [Hungarian] government's current policy has been its extreme cautiousness--as if the new political class is unwilling to call upon society to make the sacrificies that will necessarily accompany measures that address the fundamental problems of the economy.(47)

One obvious problem in developing a thorough and consistent economic strategy is the scope of economic difficulties: the problem of where to start. There are also significant external factors which limit Hungary's policy choices. Because of its large foreign debt and its links to the IMF, for instance, Hungary will come under external pressure to implement a restrictive fiscal and monetary policy.

There are, however, important internal constraints which also limit economic policy choices. Hungarian political parties do not have deep roots in Hungarian society, and this lack of depth will make it difficult for any party to mobilize the public support necessary to implement a comprehensive economic policy. Bruzst and Stark argue:

> Parties have developed in hothouse atmospheres, in which transition from social movements to political parties can be measured in months rather than years. If, for a decade or more, some of their leaders had been courageously calling on the state to change its ways, the period in which they addressed society and mobilized it for a confrontation with the state was very brief; and the week when this mobilization reached its crescendo, on 16 June 1989, was the same week it began rapidly to subside. The summer of 1989 was not a season of organizing society, but a time of negotiating with other political parties, while the fall and winter were devoted to electoral campaigns. . . . Moreover, despite their short life and their shallow roots, the new political parties in Hungary have been remarkably successful in filling the entire political space. But this almost totalizing supremacy of party politics finds the society unorganized and still lacking intermediary forms of political organization, such as trade unions, corporatist institutions or broad social movements.(48)

The lack of intermediate political organizations and the weak links between Hungarian society and political parties, make political cautiousness necessary. Arguably, the weakness of Hungarian civil society and its lack of ties with the newly organized political parties facilitated initial political institutional change, but will now hinder attempts to effect deeper economic and political changes.(49)

These domestic limits are further compounded by the effects of general political apathy. Pessimism and a feeling of inability to effect any change have left many Hungarians simply uninterested and uninvolved with political issues.(50) Eniko Tegyi writes,

> Hungarians are full of pessimism. Asked about their experiences since their "silent revolution" in 1989, they emphasize gloom: the whole economy seems to have broken down, all at once.
>
> What the Hungarians have experienced from the changes is not a striking difference in the freedom of speech, but a striking difference in working and living conditions.(51)

Hungarians are watching the economy and their own security crumble and, although some Hungarians have benefited economically from the changes, most have seen a deterioration in their living standards.(52) Resentment is also growing because of what many people view as a government sellout of Hungarian companies to foreign capital.(53) Finally, which Hungarians seem to be benfitting from the changes? Bruner writes,

> Many people brood about yesterday's communist nomenklatura becoming today's noveau riche. "Those in positions of power in the previous regime had networks in place and were the first ones to skim off the cream," Modley said. "Many Hungarians feel that nothing's really changed. The people who were in power are still in power. They now own private businesses. After all, who is the western investor going to approach when it was first possible to approach anyone? People who've had experience dealing with western firms. Who were those people? The people with power and authority in the previous regime. . ."(54)

"Democracy" and the capitalist welfare state in the West have been able to operate with relatively low participation rates, and have not yet ground to a halt because of political apathy. Both the promotion and sustaining of market socialism, however, require mass political participation and active intermediate political groups. Currently, in Hungary, democracy and the capacity of any political party to effect greater change (economically or politically) are limited by general political apathy.

In Hungary the greatest obstacles to market socialism are neither a "profound revulsion" of a role for the state nor an acceptance of monetarist prescriptions. Indeed, the ideological orientation of Hungarians is arguably more conducive to market socialism than to capitalism. As was earlier noted, it is foolish to believe that socialist principles such as equality and employment guarantees are now meaningless for the peoples in Eastern Europe. Although speculative, most Hungarians would prefer to maintain certain social democratic principles and have not suddenly transformed into classical liberals. A strong "liberal" ideology has not taken root in Hungary and this is reflected in the platforms of Hungary's political parties. Kovacs argues,

> Even the more radical reform concepts do not rely on a profound philosophical (ethical) basis, on strong arguments about the intrinsic "beauties" of the market and the virtues of private property, that is, on a radical liberal dream. Instead, the [Hungarian] reformer sees the market in a pragmatic-utilitarian way as a device for "repairing" the Soviet-type economy.(55)

Hungarians, and most East European peoples, are getting a strong, rapid dose of uncertainty and insecurity--a first taste of the precarious capitalist adventure. "Cultural revulsion" towards capitalism and the negative externalities that it generates are important factors which lead to political demands for change.(56) In Eastern Europe, where people are accustomed to security and equality is viewed as a worthwhile end, political demands for control of the market are more likely to evolve than in the West (that is, where functioning capitalist markets have led to general cultural and political acceptance).(57) That a social and political backlash will develop in Eastern Europe in response to economic hardships is not an unreasonable prediction.

While the people of Hungary desire a more efficient economy that is geared towards satisfying consumer demand, this does not further imply that a capitalist market is also desired. Kornai argues, "People [Hungarians] must change their way of thinking. Enrichment has long been considered something shameful. A fallacy has reached the marrow of people's bones: if someone gets more then it is because he took it away from others."(58) What Kornai wants to see is "enterprise" or a willingness by Hungarians "to take risks and to invest their money and wealth," to add to their own incomes and to contribute to the good of all because "national welfare is but the sum total of individual welfares."(59) Kornai wants to see a liberal ideology take root in Hungary; but why is it necessarily a problem for people to view equality, for instance, as generally desirable? Kornai would likely reply that the problem lies in an equity-efficiency tension or trade-off: levelled incomes weaken the material incentives that lead to efficient economic performance. Kornai points to this trade-off as an important reason for the failure of past Hungarian reform attempts. Kornai writes,

> The managers and workers of firm H will feel that the established proportions of earnings are "unjust". It is not because of their poor work that they have little or no profit--why then should they be punished? Therefore, they try to put pressure upon higher authorities to equalize earnings. The higher authorities themselves often feel that it is wrong to tolerate any serious inequality, since that would contradict the egalitarian traditions of the socialist movement and the acknowledged principle of "equal pay for equal work."(60)

Political pressure for equalized wages, argues Kornai, by eliminating material incentives, negatively affected the goal of improved economic performance.(61)

The tension between equality and efficiency is not, however, as straightforward as orthodox economics would suggest. Gordon, et al., correctly argue that the equality-efficiency trade-off "depends on the assumption that we are already using our resources in the most sensible way and that, as a result, the economy is a zero-sum game--more of something else means less of something else."(62) Moreover, Gordon, et al., demonstrate theoretically and empirically that greater equality does not imply that economic performance must suffer--indeed, it can improve economic performance.(63) Further, as discussed in chapter two, absolute economic equality is not a market socialist goal. The goal is to eliminate insecurity and extreme inequality. Under market socialism the market is not abandoned as a means to provide material incentives. Allowing a market implies inequality, but the degree of inequality permitted would be settled politically, not by an abstract economic analysis with questionable assumptions.(64)

Equality was/is a principle that does have meaning for Hungarians. This suggests, at the least, that social and/or cultural acceptance of capitalism may not be easy to attain in Hungary. Moreover, it would also seem that a political culture conducive to the development of market socialism may be present. Privatization and marketization (liberalization) are viewed as necessary, but so is intervention by the state. "Liberalization" in Hungary does not automatically imply that a role for the state is denied or that capitalism is the desired end. Given the general ideological background of Hungarians, it is not unrealistic to expect social demands for political control of the market (and the process of marketization) to promote general social goals over particular or individual economic interests. That is, it is not unrealistic if public debate can be initiated and political apathy reduced.

IV. CONCLUSION

> We are certainly going to see a litle more leeway for free enterprise and stronger market orientations by necessity and by default of the old planning apparatus; but very pragmatic, very partial, and politically not very well anchored markets. Or, to conclude as we began with Adam Smith: "To expect, indeed, that the freedom of trade should ever be entirely restored . . . is as absurd as to expect that an Oceana or Utopea should ever be established.(65)

As this chapter has argued, marketization in Hungary is pragmatically viewed as a necessary process. Hungarians have not suddenly transormed, en masse, into radical capitalists, as the Western media tend to suggest. A past obstacle to economic reform in Hungary--a centralized political system--has been eliminated. The failure of past reform in Hungary, however, has left many doubtful about the viability of market socialism. These doubts about market socialism are arguably misplaced as market socialism cannot work, as Chapter two argued, within a monohierarchical system.(66) Nevertheless, uncertainty about market socialism has not also persuaded Hungarians that capitalism is the answer. Instead, social democratic, not classical liberal, best describes the predominant ideological force in Hungary.

The limits to fostering market socialism in Hungary are neither ideological nor the absence of political debate or support for an alternative development model. A major problem, however, is widespread political apathy. Political apathy will make it difficult to stimulate intermediary political organizations, and to increase ties between

Hungarian political parties and civil society. All East European states need to implement a comprehensive industrial policy to direct prudently the transformation. But the weak social foundations that Hungarian political parties rest on makes it difficult for any party to mobilize the support necessary to introduce a broad-ranging economic policy.

The old system is crumbling, but, to date, attempts to direct and promote a new system have been limited. The lack of policy and the extreme cautiousness of policymakers in Hungary are unavoidable given the weak links between Hungarian society and political parties. This is a vicious circle that will be difficult to break: lack of policy will worsen not improve the general economic situation for most Hungarians, in turn, increasing political apathy and resentment.

CONCLUSION: A SEMI REVOLUTION(1)

> In the late 1980s, the Hungarian economy exhibited a number of serious negative phenomena, both social and economic. On the social level the chronic housing problem, the very long hours of work (resulting from the second and third jobs of state economy employees), alcoholism, morbidity and poverty were all serious problems. On the economic level, stagnant or declining real wages throughout the 1980s (at any rate if state sector income is only considered), inflation, balance of payments deficit and growing foreign debts were all major problems.(2)

Strengthening the economy is Hungary's new political leaders most urgent and pressing problem. Economic strategies adopted now will directly affect immediate, tangible conditions for Hungarians, and, more generally, the long term evolution of economic and political institutions. All East European states must promote marketization and stabilization--the crucial question is how. A rapid liberalization strategy, which its proponents hope will lead to "capitalism" and an open, competitive economy, is limited for economic, political, and social reasons. The negative short-run impact of a rapid strategy makes it politically unsustainable. In the long-run, moreover, it would do little to improve the position of most East European peoples. A rapid marketization approach would simply transfer ownership of the bulk of state-owned assets to either foreign capital or to old party nomenklatura.

The alternative, a gradualist marketization strategy, is admittedly vague and opaque: its focus is domestic development and its outcome is uncertain. It is certain, however, that a rapid strategy cannot succeed. Further, if we compare the social costs of a rapid versus a gradualist strategy, then it is evident that the latter is preferable. Given the scale and inherent difficulties of the economic transformation, a cost-minimization criterion is arguably appropriate. We should not ignore the social and political impact of economic policies nor forget that "democracy" is also a valued East European goal. Economic inequality and a continuing deterioration in living standards will hinder attempts to promote greater democratization.(3)

In Hungary there exists significant political support for an alternative development strategy: the third way. A third way strategy is aware of and concerned with distributional and social questions. It favours fostering the development of the domestic private sector--along side of the state sector (which is not dismissed a priori as inefficient and unnecessary). A third way strategy, if successful, would lead to a dual economy, similar to the one outlined in chapter two, and could be considered market socialist. Even if a third-way strategy is not intentionally promoted, the size of the state sector, the difficulties of disinvestment, and the need for public goods all suggest a continuing role for the state in the economy. Finally, in Hungary, there is no prominent political party with a radical neo-liberal agenda. Indeed, social democratic seems to be the predominant ideological force not classical liberal. A role for the state is not ideologically rejected by Hungary's major political parties, nor has the market as saviour been whole-heartedly embraced.

> Although the Third Way corresponds to the [Hungarian] government's domestic constituency and its political exigencies, modified Thatcherism more closely reflects the preferences of its international constituency and its economic exigencies. Hence, it would hardly be surprising if the government seeks to straddle the two approaches, using neoclassical orthodoxy in its approach to stabilization while adhering more closely to a Third Way strategy in its approach to structural reform issues.(4)

In Hungary a combination of rapid and gradual strategies is not unlikely nor should it be surprising. The most salient feature of future Hungarian economic strategy, however, could be the lack of economic policy; or stabilization without accompanying restructuring measures. A major problem for new political parties in Hungary is their inability to mobilize popular support, necessary for the introduction of broad-ranging changes. The weak ties between Hungarian civil society and political parties, and general political apathy are crucial factors which will negatively effect the evolution of economic policy. Furthermore, uncontrolled marketization will lead to further political apathy and disenchantment as only a minority of Hungarians would benefit economically. Bruner writes,

> "Sometimes [Hungarian entrepreneurs] don't have to circumvent [rules and regulations], because sometimes the regulations don't exist. In fact, we have established a private economy without regulations. It's a jungle . . ." [said Matyas Vince, a journalist who has been editor of the three most successful business periodicals in Hungary.]
>
> The rulers of the jungle are already sharpening their claws. Economist Gyorgy Matolcsy believes "plutocrats" will own as much as 25% of all property in Hungary by the year 2000.(5)

Who are these plutocrats likely to be? As was discussed, those in a position to gain were those in power when the changes were first introduced. Not only are its distributional consequences undesirable, but lack of policy will also make it continually more difficult to manage effectively the large state sector. Fiscal positions will continue to deteriorate as will economic performance: capital stock will become older and more obsolete, and infrastructures will become increasingly costly to develop.

The Western media is inaccurate when it portrays Hungarians as "capitalists". Historical, social and cultural conditions are different than those in the West, as are attitudes regarding the roles of the market and the state. Economic limits and political beliefs suggest that market socialism is a possibility in Hungary. The greatest obstacle to reform in Hungary is widespread political apathy. Although it is impossible to foresee Hungary's future, we can argue, with a great deal of certainty, that a Western-capitalist structure will not evolve. It also seems certain that if Hungary cannot implement a gradualist marketization strategy and an active state-directed restructuring policy, then the majority of Hungarians will continue to suffer under a withering economy.

FOOTNOTES

INTRODUCTION

1 The first difficulty that arises is what to call the states in "Eastern" Europe. Some prefer East Central or Central Europe, but this essay will use Eastern Europe to denote Poland, Hungary, Romania, Bulgaria and Czechoslovakia. Further, I make no attempt to include what used to be the Soviet Union in this analysis. The differences between the Soviet area and Eastern Europe now outweigh the similarities.

2 The editor of the Journal of International Affairs argues: "Both reformed communists and former opposition figures now face economic crises of ever-growing magnitude. Where 'shock therapy' conversions to the market may have looked quick and simple, though painful, on paper, they have been extraordinarily complex and confusing for both economists and politicians." "Editor's Foreword," Journal of International Affairs. Vol. 45, No. 1, pp. iii-iv.

3 Gyorgy Balo and Ivan Lipovecz, eds., (1991). Tenyek Konyvo. Budapest: Alfoldi Ryomda, pp. 19-20 and p. 613. (Translated, from Hungarian to English, by Andrea Verlag.)

4 Ibid. Michael Meyer writes "'Everywhere there is poverty--beggars on the street, people sleeping in the subways, shops full of goods that no one can afford [Andras Hirschler, Director of Investcenter].' Two of three Hungarians are having trouble making ends meet; living standards are nose-diving, breeding social unrest." Michael Meyer (1992), "Goulash Capitalism," Newsweek. January 13, 1992, p.20. (Despite Meyer's recognition that the social costs are high, he still views the changes underway in Hungary as very positive, wonderful, exciting . . .)

5 Laszlo Bruszt and David Stark (1991), "Remaking the Political Field in Hungary: From the Politics of Confrontation to the Politics of Competition," Journal of

International Affaris. Vol. 45, No. 1, p. 210.

6 Richard W. Bruner (1991), "The Price of Change," Budapest Week. October 24-30, 1991, p. 7.

7 Arguably there are only two approaches because East European states do not yet have the luxury, for instance, to think about whether they desire a strong or weak welfare state. Current policy will affect future structures, but presently the main objective will be keeping afloat while promoting marketization. For a good discussion on economic policy limits, see Ellen Comisso (1991a), "Political Coalitions, Economic Choices," Journal of International Affairs. Vol. 45, No. 1.

8 I will examine the implications of a third way (or gradualist) approach in chapter two, and will look at who the third "wayers" are in chapter three.

9 How liberalism is viewed, at least in Hungary, will be developed in chapter three.

10 There is a great deal written on the NEM. Articles and books by Janos Kornai are particularly good references. For example, see Janos Kornai (1986), Contradictions and Dilemmas: Studies on the Socialist Economy and Society. Cambridge, Massachusetts: The MIT Press.

11 On the limited nature of the NEM, see Ellen Comisso and Paul Marer (1986), "The Economics and Politics of Reform in Hungary," International Organization. Vol. 40, No. 2; I. T. Berend (1989), "The Crisis of the Hungarian Reform in the 1970s," Acta Oeconomica. Vol. 40, Nos. 1-2; and, L. Szamuely (1989), "Intentions and Constraints: Reflections on Reading Ivan T. Berend's Study," Acta Oeconomica. Vol. 40, Nos. 1-2.

12 For some statistics on the size, role, and nature of Hungary's private sector or second economy see Bruno Dallago (1989), "The Non-Socialized Sector in Hungary: An Estimation of its Importance," Yearbook of East-European Economics. Munich: Gunter Olzog Verlag, Vol. 13, No. 2.

13 The centralized economies used to include the

Soviet Union, Hungary, Poland, Romania, Czechoslovakia, Bulgaria, (and East Germany).

14 Wlodzimierz Brus (1972), The Market in a Socialist Economy. London: Routledge & Kegan Paul, pp. 65-71.

15 Michael Ellman (1989), Socialist Planning (second edition). Cambridge: Cambridge University Press, p. 19. Monohierarchical: a combination of state ownership of the means of production and political dictatorship.

16 Ibid., p. 24.

17 Ibid., p. 22.

18 On economic behavior in the centralized model see: Michael Ellman (1989), Socialist Planning, second edition. Cambridge: Cambridge University Press; Alec Nove (1983), The Economics of Feasible Socialism. London: George Allen & Unwin; and, Janos Kornai (1986), Contradictions and Dilemmas: Studies on the Socialist Economy and Society. Cambridge, Massachusetts: The MIT Press.

19 See Janos Kornai (1986), op.cit.

20 Janos Kornai (1980), "The Dilemmas of a Socialist Economy: The Hungarian Experience," Cambridge Journal of Economics. Vol. 4, No. 4, p. 152.

21 For a good summary on the nature of and the reasons for the shortage economy see Alec Nove (1983), The Economics of Feasible Socialism. London: George Allen & Unwin.

22 Ibid., pp. 71-2.

23 On the negative effects of overinvestment, see Ellman (1989), op.cit. In particular, pp. 154-69.

24 Ibid., p. 163.

25 Ibid.

26 Ibid., p. 138.

27 Ibid., p. 151.

28 Paul Marer (1991), "The Transition to a Market Economy in Central and Eastern Europe," The OECD Observer. No. 169, April/May 1991, p. 5. On obsolecsent capital stock: "In [Hungarian] industry, for example, the share of assets less than five years old declined from 41 percent in 1975 to 24 per cent in 1987. Moreover, the nation's aging capital stock was poorly maintained." Secretariat of the Economic Commission for Europe (1990), Economic Survey of Europe in 1989-90. New York: United Nations Publication, p. 245.

29 Secretariat of the Economic Commission for Europe (1991), Economic Survey of Europe in 1990-91. New York: United Nations Publication, p. 75, and see pp. 74-82.

30 Paul Marer (1991), op.cit., p. 5.

31 Ibid.

32 For an overview of Hungary's past economic performance see the Secretariat of the Economic Comission for Europe (1990 and 1991), op.cit.

33 Ellen Comisso and Paul Marer (1986), "The Economics and Politics of Reform in Hungary," International Organizations. Vol. 40, No. 2, p. 444.

34 Ibid., p. 425.

35 L. Szamuely (1989), "Intentions and Constraints: Reflections on Reading Ivan T. Berend's Study," Acta Oeconomica. Vol. 40, Nos. 1-2, p. 154.

36 I. T. Berend (1989), "The Crisis of the Hungarian Reform in the 1970s," Acta Oeconomica. Vol. 40, Nos. 1-2, p. 132.

37 Ibid., p. 115.

38 Hungary's economy in the 1970s and 1980s cannot be considered market socialist. Although Hungary introduced what seemed to be substantial changes, its system was still

a version of the centralized model. See Bela Csikos-Nagy Comments in Schuller's (1988) Does Market Socialism Work? London: The Centre for Research into Communist Studies, p. 69. In particular, Nagy correctly argues that the organization of the economic system was dominated by vertical rather than horizontal exchange relations, and there were neither labour nor capital markets. Ibid., p. 115.

39 For a general survey of "socialism" see Bernard Crick (1987), Socialism. Minneapolis: University of Minnesota Press.

40 "Market socialism" will be defined and discussed in chapter two.

41 Wlodzimierz Brus (1972), op cit., pp. 137-38.

42 Ellen Comisso (1991a), op.cit., p. 1.

43 The reasons for what often seems to be a no-policy approach and its effects will be considered in chapter three.

CHAPTER ONE: ECONOMIC CATASTROPHE AS REVOLUTION

1 Jeffrey Sachs (1990), Eastern Europe's Economies: What is to be Done?" Comparative Politics 90/91, Eighth Edition. Guilford, Connecticut: The Dushkin Publishing Group.

2 Poland followed Sachs's formula and it seems that Russia will also take this route despite the great uncertainty regarding success: "'The expectations [about Russia's economic performance] should be kept very low,' counsels Swedish economist Aslund. 'Anything that is less than complete chaos must be considered a success.'" "Yeltsin Rolls the Dice," International Business Week, December 16, 1991, p. 20.

3 Orthodox refers to a "mainstream" or "textbook" economic analysis. It is characterized primarily by its abstract analysis and its lack of attention to social and political factors: economics is studied within a stylized market structure.

4 Jeffrey Sachs (1990), op.cit.

5 Ibid.

6 Ibid., p. 153.

7 Ibid., p. 154.

8 Sachs uses a rational expectations approach which broadly is a theoretical attempt to link micro and macro economic levels. This approach not only argues that unemployment is necessary, but it is also influential in Sachs's emphasis on rapidity. Simon, who advocates the same policy as Sachs, writes: "In order to avoid that expectations work against macroeconomic policy, policy must be implemented completely and immediately. If consumer prices are set at their final value overnight, no expectations of further increases are justified." A. Simon (1990), "Eastern Europe's movement Towards Capitalism: Hard Landing or Soft Landing?" Acta Oeconomica. Vol. 42, Nos. 1-2, p. 45. Such an approach, Simon and Sachs believe, will not only lead to real prices, but will also eliminate inflationary pressures.

9 Jeffrey Sachs (1990), op.cit., p. 154.

10 In orthodox economic theory the economy is isolated from social and political institutions. Indeed, the market itself is portrayed in a highly abstract manner. For instance, the number of firms defines the market structure: a market is competitive if there are many firms. This abstract, narrow perspective is a common Marxist criticism of orthodox analysis. See, for instance, John Weeks (1981), Capital and Exploitation. Princeton: Princeton University Press.

11 Richard Bruner writes "To a great many Hungarians, these changes are bewildering beyond comprehension. The

other day, a sad-voiced woman phoned a radio talk show to express her conviction that the 1960s were better for Hungary than the present." With the combination of insecurity and uncertainty and growing poverty, this attitude is probably not unusual. See Richard Bruner (1991), "The Price of Change," *Budapest Week*. October 24-30, 1991, p. 7.

12 Secretariat of the Economic Commission for Europe (1991), *Economic Survey of Europe in 1990-1991*. New York: United Nations Publication, p. 119.

13 Jeffrey Sachs, *op.cit.*, p. 154.

14 Ibid.

15 Richard C. Longworth (1990), "E.C. Fosters change in Eastern Europe," *Europe*. November, 1990, p. 25. Also see this issue for aid packages that the EC has outlined for Eastern Europe.

16 Although autarky is not a Hungarian option, the type of international economic strategy that it follows is important. To believe that Hungary can successfully promote an economic strategy like that of the NICs is unrealistic. An export-led growth strategy (with a West European focus), however, is what Sachs's policy suggests.

17 Deborah Milenkovitch (1991), "The Politics of Economic Transformation," *Journal of International Affairs*. Vol. 45, No. 1, p. 163.

18 Jeffrey Sachs, *op.cit.*, p. 155.

19 Policy reversals in Poland demonstrate this. See, for instance, Stanislaw Wellisz (1991), "The Lessons of Economic Reform: The Polish Case," *Journal of International Affairs*. Vol. 45, No. 1.

20 Ibid.

21 Ellen Comisso (1988), "Market Failures and Market Socialism: Economic Problems of the Transition," *East European Politics and Societies*. Vol. 2, No. 3, p. 447.

22 Ibid., p. 448.

23 Ibid., pp. 448-9.

24 Ibid., p. 449.

25 Ibid., p. 450.

26 Ibid.

27 On the negative effects of neither plan nor market (primarily, a rapid increase in demand for imports and massive borrowing by state-owned enterprises), see, for example, Tamas Bauer (1988), "Hungarian Economic Reform in East European Perspective," East European Politics and Societies. Vol. 2, No. 3.

28 Secretariat for the Economic Commission of Europe (1991), op.cit., p. 158.

29 Ibid.

30 Ibid.

31 Jeffrey Sachs (1990), op.cit., p. 153.

32 Tardos in Comisso (1988), op.cit., p. 153.

33 Ibid.

34 See Comisso (1988), op.cit., p. 451.

35 On the political exceptions and exemptions (or political bailouts) which prevented market adaptation, see the Introduction, pp. 15-16.

36 Tardos in Comisso (1988), op.cit., pp. 450-1.

37 See Csikos-Nagy Comments in Alfred Schuller (1988), Does Market Socialism Work? London: The Centre for Research into Communist Economies, p. 69.

38 For information on Hungary's second economy, see the Yearbook of East-European Economics (1989). Munich:

Gunter Olzog Verlag, Vol. 13, No. 2.

39 Ellen Comisso (1988), *op.cit.*, pp. 440-1.

40 Secretariat for the Economic Commission of Europe (1991), *op.cit.*, p. 133.

41 David Stark (1990), "Privatization in Hungary: From Plan to Market or from Plan to Clan," *East European Politics and Societies*. Vol. 4, No. 3, p. 352.

42 Janos Kornai (1990), *The Road to a Free Economy*. New York: W.W. Norton & Company, p. 56.

43 Peter Akos Bod (1990), "A Roundtable on Privatization," *New Hungarian Quarterly*. Vol. 31, No. 117, p. 94.

44 If a rapid privatization strategy is promoted, then reliance on foreign capital is necessary because of the lack of domestic capital. David Stark writes, "Given the ratio of public assets to private savings (most estimates are that private domestic savings, even with credit, could buy only about 10 percent of current state assets), and given the weight of convertible currency foreign debt, rapid sales of state enterprises would tend to favor foreign buyers." David Stark (1990). *op.cit*., pp. 370-1.

45 Steve Dryden (1990), "Investing in Eastern Europe," *Europe*. January/February, 1990, p. 24.

46 Ibid.

47 Ivan Szelenyi (1990), "Alternative Futures for Eastern Europe: The Case of Hungary," *East European Politics and Societies*. Vol. 4, No. 2, p. 250.

48 David Stark (1990), *op.cit.*, pp. 370-1.

49 See "A Roundtable on Privatization," *New Hungarian Quarterly*. Vol. 31, No. 117; and, Irena Grosfeld (1991), "Privatization of State Enterprises in Eastern Europe: The Search for a Market Environment," *East European Politics and Societies*. Vol. 5, No. 1.

50 Secretariat for the Economic Commission of Europe (1991), op.cit., p. 160.

51 Ibid.

52 Istvan Csillag (1990), "A Roundtable on Privatization," New Hungarian Quarterly. Vol. 31, No. 117, p. 92.

53 On semi-privatization in 1984, see David Stark (1990), op.cit.,; and, M. Tardos (1989), "Economic Organizations and Ownership," Acta Oeconomica. Vol. 40, Nos. 1-2.

54 Janos Martonyi (1990), "A Roundtable on Privatization," New Hungarian Quarterly. Vol. 31, No. 117, p. 91.

55 Peter Akos Bod (1990), op.cit., p. 93. For a defence of spontaneous privatization see Gy Matolcsy (1990a), "Defending the Cause of Spontaneous Reform of Ownership," Acta Oeconomica. Vol. 42, Nos. 1-2.

56 Peter Akos Bod (1990), op.cit., p. 92.

57 Janos Martonyi (1990), op.cit., p. 92.

58 Ibid.

59 See J. A. Schumpeter (1975). Capitalism, Socialism, and Democracy. New York: Harper Torchbooks.

60 Monopolies in a capitalist system operate within a market and their decision-making is affected by the market's operation. See Auerbach, et al. (1988), "The Transition from Actually Existing Capitalism," New Left Review. No. 170, July/August 1988.

61 Peter Akos Bod (1990), op.cit., p. 95.

62 David Stark (1990), op.cit., p. 371.

63 Ibid., p. 372.

64 Ibid., p. 373.

65 Ibid., pp. 373-4.

66 Ibid., p. 375.

67 Ibid.

68 Ibid., pp. 377-8.

69 This is a socialist argument or position which challenges the liberal assumption that an atomized market maximizes social welfare. The concept of "market socialism"--a controlled market--will be developed in the next chapter.

70 See David Stark (1990), op.cit., p. 380; and, Ivan Szelenyi (1990), op.cit. Related to dispersed ownership is the issue of employee operated (owned) enterprises. There is a great deal of literature on this--see, for instance, L. Neumann (1990), "Small Business Off-Shoots from Large Manufacturers--A Privatization Option," Acta Oeconomica. Vol. 42, Nos. 1-2.

71 Ivan Szelenyi (1990), op.cit., p. 250.

72 David Stark (1990), op.cit., p. 388.

73 Ibid., p. 389.

74 Ibid., p. 391.

75 Ibid., p. 392.

76 Ivan Szelenyi (1990), op.cit., p. 248.

77 Ibid., p. 247.

78 Ibid., p. 252.

CHAPTER TWO: MARKETING SOCIALISM

1 Ivan Szelenyi (1990), op.cit., p. 232.

2 See Alec Nove (1983). The Economics of Feasible Socialism. London: Allen & Unwin.

3 Ellen Comisso (1991), "Property Rights, Liberalism, and the Transition from 'Actually Existing' Socialism," East European Politics and Societies. Vol. 5, No. 1, p. 179.

4 Political reasons for believing that a social democrat rather than a liberal ideology will predominate, will be developed in chapter three.

5 Lou Ferleger and Jay R. Mandle (1990), op.cit., p. 127.

6 Michael Harrington (1989), "Toward a New Socialism," Dissent. Spring, 1989, p. 70.

7 Competition is the beauty and beast of capitalism. Competition is what gives capitalism its innovative character--its ability to revolutionize the means of production from within. Competition, however, also leads to uneven development, economic crisis and the concentration and centralization of capital. Both Marx and Schumpeter, for instance, pointed to the socially disruptive nature of capitalism (Schumpeter, of course, highlighted the benefits gained by this process: "creative destruction"). See Joseph Schumpeter (1975), Capitalism, Socialism, and Democracy. New York: Harper Torchbooks. Alec Nove writes: "One sees, in varying degrees, the social-political unacceptability of rapid transformation of societies in the name of private profit, where highly imperfect markets and uneven development enable some individuals to grow very rich indeed while the very poor remain very poor." Alec Nove (1983), The Economics of Feasible Socialism. London: George Allen & Unwin, p. 6.

8 Generally, a welfare state is social policy plus a (fundamentally unaltered) capitalist market. Market

socialism, by intervening in the market, changes significantly the market's operation. For instance, it would change the social conditions under which the wage bargain is made. See this chapter, pp. 69-70. Admittedly, this is a rather vague criterion. For example, where does Sweden with its active social-labour policy, or France with its active state industrial policy, fit in? It is impossible to draw a theoretical line, I think, distinguishing welfare-state capitalism and market socialism. Instead, consideration of economic policy and ideological beliefs of concrete cases tends best to suggest appropriate categories.

9 Welfare state proponents do not challenge the basic underlying liberal assumptions which portray the unfettered market as the best means to promote social goals. Social policy may assist those who are negatively affected by the operation of the capitalist market, but it does not alter the conditions or social relations which lead necessarily to the generation of these negative externalities.

10 Ibid. A welfare state falls under the capitalist category because it does not intervene to control meaningfully the market, as it is believed that a uncontrolled market is economically and politically superior.

11 Ellman writes that Marxism stresses the two following advantages that socialism has vis-a-vis capitalism: "First the absence of the anarchy of production, and secondly the absence of class conflict." Ellman (1989), op.cit., p. 8. Socialists challege basic liberal assumptions by arguing that what is rational behavior for an atomistic firm (or individual) is often irrational for society as a whole. The classical liberal argument portrays the relationship between the individual and society as harmonious: there is no conflict, hence an improvement for one is an improvement for all. But, externalities are decisive in a critique of capitalism, and favour arguments for socialism. Externalities are caused by market failure and occur when costs (and benefits) are not captured completely by the market exchange mechanism. Pollution is an illustrative example. Viewing both costs and benefits from a social standpoint, theoretically, internalizes

externalities by properly measuring the value of their indirect and direct social effects.

12 See, for instance, Bernard Crick (1987), Socialism. Minneapolis: University of Minnesota Press.

13 Alec Nove (1983), op.cit., p. 200.

14 Ellen Comisso (1989), "Property Rights in Focus," Acta Oeconomica. Vol. 40, Nos. 3-4, p. 211.

15 Ibid.

16 Ibid.

17 Lou Ferleger and Jay R. Mandle (1990), "The Economic Future of Socialism in Eastern Europe," Socialist Review. Vol. 20, No. 2, p. 128.

18 Ibid., p. 130.

19 The notion that market socialism is more than a technical issue will be developed in chapter three.

20 Alec Nove (1983), op.cit., p. 227.

21 Ibid., pp. 221-2.

22 We will examine the effects of non-controlled marketization in chapter three.

23 See Wlodzimierz Brus (1973), The Economics and Politics of Socialism. London: Routledge & Kegan Paul; and, Alec Nove (1983), op.cit.

24 Saul Auerbach, et al., (1988), "The Transition from Actually Existing Capitalism," New Left Review. No. 170, July/August, 1988, p. 73.

25 Ibid., pp. 63-65. For Mandel's argument see "In Defence of Socialist Planning," New Left Review. No. 159, September/October 1986.

26 Ibid., in particular, see p. 62 and p. 75.

27 Ibid., p. 75.

28 Ibid.

29 Ibid.

30 Ibid., p. 76.

31 Michael Harrington (1989), op.cit., p. 69.

32 Ibid.

33 David Miller and Saul Estrin (1987), "A Case for Market Socialism," Dissent. Summer, 1987, p. 365.

34 Ernest Mandel (1988), "The Myth of Market Socialism," New Left Review. No. 169, May/June 1988, p. 114.

35 Ibid.

36 Ibid., p. 118.

37 Ibid.

38 Ibid., pp. 118-9.

39 Ernest Mandel (1986), "In Defence of Socialist Planning," New Left Review. No. 159, September/October 1986, p. 28.

40 Michael Harrington (1989), op.cit., p. 178; and, see Auerbach, et al., (1988), op.cit., p. 78.

41 John Dunn (1984), The Politics of Socialism: An Essay in Political Theory. Cambridge: Cambridge University Press, p. 31.

42 See Carl Von Clausewitz (1984), On War. Edited and Translated by Michael Howard and Peter Paret. Princeton: Princeton University Press. In particular see Chapters 4-7 (Book 1). Friction: "Countless minor incidents--the kind you can never foresee--combine to lower the general level of performance, so that one always falls short of the intended

goal." p. 119.

43 Ibid. It is the "human element" which causes friction.

44 Ibid.

45 An example is the use of "short-lines" in Saskatchewan which are privately owned and operated rail companies (which do show a profit) to service those areas that monopoly railway companies find unprofitable and will not service. Without short-lines, many areas in Saskatchewan would not have easy access to rail transportation. A monopoly company (private- or public-owned) could service these areas and finance losses through cross-subsidization; yet, this is arguably a waste of resources and unnecessary.

46 Ernest Mandel (1986), op.cit., pp. 21-22. In particular, Mandel is concerned with the despotism over producers--labour--if a market is allowed to operate.

47 David Miller and Saul Estrin (1987), op.cit., p. 366.

48 Ibid., p. 361.

49 Michael Harrington (1989), op.cit., p. 66.

50 Ibid., pp. 64-66.

51 Ibid., p. 65.

52 Ibid., p. 57.

53 Ibid.

54 Ibid.

55 A neoclassical or rational expectations economist would reject this; but, I think that this is a political/social issue that requires consensus and cooperation. It is not strictly an economic problem in the sense that it would not negatively affect the operation of

the "market" (the example of Sweden--a small and open economy--does demonstrate this). Of course, reaching such a consensus and inducing cooperation are not easy--but this is a separate issue.

56 Alec Nove (1983), op.cit., pp. 221-2.

57 Saul Auerbach, et al, (1988), op.cit., p. 78.

58 Ellen Comisso (1989), op.cit., p. 214.

59 Ibid., p. 213.

60 David Miller and Saul Estrin (1987), op.cit., p. 361.

61 Ellen Comisso (1989), op.cit., p. 213.

62 Some of the difficulties under capitalism include: socially undesirable investment; lack of investment; investment that focuses--too much--on the short-run and immediate interests; the "casino-like" nature of capitalism; etc.

63 Janos Kornai (1990), op.cit., p. 51.

64 Ellen Comisso (1991), op.cit., p. 164.

65 Ibid., p. 172.

66 Ibid., p. 169.

67 Ibid., p. 168.

68 Ibid., p. 169.

69 Ibid., pp. 168-72.

70 Ibid.

71 Ibid., p. 164.

72 Non-exclusion principle: "individuals and groups have the right freely to use property as they wish, and no

one is excluded from doing so." Ibid., p. 167.

73 Ibid., pp. 167-8.

74 Ibid., p. 171.

75 Ibid., p. 172.

76 Ibid., pp. 172-3.

77 Ibid., p. 173.

78 Ibid.

79 Ibid., p. 167.

80 Ibid. One example of a successful publicly-owned enterprise in Hungary was Tunsgram--see page 40.

81 Ibid., pp. 174-5.

82 One possible way of promoting genuine economic behavior, or inducing ownership roles, is to pluralize public owners. As outlined in Chapter one, non-profit institutions such as hospitals, would hold shares in state-owned enterprises and would receive their endowments or revenues from these enterprises. Shareholders would then have a real interest in ensuring that enterprise behavior was economically sound. See Marton Tardos (1989), "Economic Organizations and Ownership," Acta Oeconomica. Vol. 40, Nos. 1-2. Also, the arguments developed by Auerbach, et al., indicate that the existence of monopolies (publicly-owned under market socialism) does not imply that competition or the market are necessarily sacrificed. See Auerbach, et al. (1988), op.cit.

83 This criticism is important because the failure of past reform attempts in Hungary have left many Hungarians very skeptical about the viability of market socialism--for example, see Janos Kornai(1990), op.cit.

84 Ellen Comisso and Paul Marer (1986), "The Economics and Politics of Reform in Hungary," International Organization. Vol. 40, No. 2, p. 444.

85 L. Szamuely (1989), "Intentions and Constraints: Reflections on Reading Ivan T. Berend's Study," Acta Oeconomica. Vol. 40, Nos. 1-2, p. 155.

86 Ibid., p. 158.

87 For this section, I rely primarily on Comisso and Marer (1986), op.cit.

88 Ibid., p. 434.

89 Ibid., p. 439.

90 Ibid.

91 Ibid.

92 Ibid., p. 440.

93 Ibid.

94 Ibid., p. 442.

95 Ibid., see, in particular, pp. 438-47.

96 Ibid., see, in particular, pp. 444-47.

97 Michael Meyer (1992), op.cit., p. 22.

98 See Deborah Milenkovich (1991), op.cit., pp. 159-160.

99 Ibid.

CHAPTER THREE: POSSIBILITIES AND LIMITS

1 John Dunn (1984), The Politics of Socialism: An Essay in Political Theory. Cambridge: Cambridge University Press, p. 92.

2 Gramsci argued that the reproduction of cultural acceptance was/is also central in maintaining the capitalist system: capitalism is more than relations of production. The argument that an economic structure is insufficient also holds for the development and sustaining of market socialism. Although this chapter does not consider Gramsci's arguments directly, it is influenced by Gramsci's analysis. See Antonio Gramsci (1989). Selections From the Prison Notebooks. Edited and translated by Quintin Hoare and Geoffery Nowell Smith. New York: International Publishers.

3 Bruszt and Stark (1991), op.cit., p. 241.

4 Ibid., and see Comisso (1991a), op.cit.

5 Bruszt and Stark (1991), op.cit., p. 231.

6 Ibid., pp. 228-231.

7 Ibid., p. 229.

8 Ibid.. p. 233.

9 Ibid.

10 Ibid., pp. 237-241.

11 Ibid., pp. 238-239.

12 Ibid., p. 239.

13 Ibid., p. 240.

14 Ibid., and see Comisso (1991a), op.cit.

15 Ellen Comisso (1991a), op.cit., p. 13.

16 Bruszt and Stark (1991), op.cit., p. 241.

17 Janos Matyas Kovacs (1991), "From Reformation to Transformation: Limits to Liberalism in Hungarian Economic Thought," East European Politics and Societies. Vol. 5, No. 1, p. 71.

18 See Mihaly Laki (1991), "Economic Programs of the Ex-Opposition Parties in Hungary," East European Politics and Societies. Vol. 5, No. 1.

19 Ibid., p. 91.

20 Andras Bozoki (1990), "Post-Communist Transition: Political Tendencies in Hungary," East European Politics and Societies. Vol. 4, No. 2, pp. 228-229.

21 I am uncertain of what Bozoki means by "value neutral". As for the advantageous positions that technocrats hold, see this chapter p. 106.

22 Ellen Comisso (1991a), op.cit., p. 4.

23 Mihaly Laki (1989), Opposition Movements and Parties on the Hungarian Economy. Budapest: The Hungarian Economic Information Service, p. 43.

24 See Ibid.

25 Ibid.

26 Mihaly Laki (1991), op.cit., p. 77.

27 Ibid., p. 76.

28 Ibid., pp. 79-80.

29 Ibid.

30 Ibid., p. 81.

31 See Ibid.; and Mihaly Laki (1989), op.cit.

32 Ibid.

33 Ibid.

34 Mihaly Laki (1991), op.cit., pp. 88-89.

35 Ibid.

36 Ibid.

37 On the current Hungarian social welfare policy, see the Secretariat for the Economic Commisson of Europe (1991), op.cit., p. 161; and the Commission (1990), op.cit., pp.153-54.

38 Szelenyi for instance is a third way advocate, but rejects "market socialism". See Szelenyi (1990), op.cit.

39 Ibid. Szelenyi promotes a dual economy and does not reject a role for the state sector.

40 See Janos Kornai (1990), op.cit.; and, Szelenyi (1990a), "Hungary 1989: An Introduction," East European Politics and Societies. Vol. 4, No. 2.

41 Ibid.

42 Ibid.

43 Budapest Week, "Newsbriefs". October 3-9, 1991.

44 Federation of Young Democrats (1991). FIDESZ: Hungary 1991. Budapest: FIDESZ Central Office; Lendvay utca 28; Budapest, 1062, p. 18.

45 On the differences between market socialism and a welfare state see chapter 2, pp. 55-56.

46 Deborah Milenkovich (1991), op.cit., p. 159.

47 Bruszt and Stark (1991), op.cit., p. 243.

48 Bruszt and Stark (1991), op.cit., pp. 242-43.

49 See Ibid.; and, Ellen Comisso (1991a), op.cit.

50 See, for example, the Introduction, p. 3.

51 Eniko Tegyi (1991), "Business in Post-Communist Hungary," Budapest Week. October 3-9, 1991, p. 7.

52 On deteriorating living standards, see Gyorgy Balo

and Ivan Lipovecz, eds. (1991), Tenyek Konyvo. Budapest: Alfoldl Ryomda, pp. 19-20 and p. 613.

53 On anger over foreign sell-outs, see Eniko Tegyi (1991), op.cit.

54 Bruner (1991), op.cit., p. 7.

55 Janos Matyas Kovacs (1991), op.cit., p. 59.

56 See John Dunn (1984), op.cit.

57 As was noted, the maintenance of capitalist relations depends on cultural acceptance, not only on the reproduction of capitalist relations of production. The cultural acceptance of capitalism (and ideological dominance of liberalism) in the West is an important reason for its continuing strength.

58 Janos Kornai (1990), op.cit., pp. 181-82.

59 Ibid., pp. 190-1.

60 Janos Kornai (1980), op.cit., p. 150.

61 Kornai's analysis is limited. Arguably, there were more important reasons for the past failure of reform: primarily the centralized political structure in Hungary.

62 David Gordon, et al. (1990), "An Equality-Efficiency Trade-Off?", Dissent. Fall, 1990, p. 510.

63 See Ibid.

64 Orthodox economics has a sterilized conception of economics and the market. Simplifying assumptions and abstract theories suggest that economic relationships are obvious and straightforward. In reality, however, the conclusions of abstract economic theories typically are inapplicable or, at least, must be scrutinized carefully.

65 Erich W. Streissler (1991), "What Kind of Economic Liberalism May We Expect in 'Eastern Europe?" East European Politics and Societies. Vol. 5, No. 1, p. 201.

66 On the importance of political limits to past reform attempts, see chapter two pp. 78-83.

CONCLUSION

1 "A Semi-Revolution" from Robert Frost's poem "A Semi-Revolution," in The Norton Introduction to Literature (1983). W.W. Norton And Company, Inc., p. 145.

2 Michael Ellman (1989), op.cit., p. 65.

3 Also, authoritarianism and capitalism, for instance, are not incompatible.

4 Ellen Commisso (1991a), op.cit., p. 26.

5 Richard W. Bruner (1991), op.cit., p. 7.

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29, No. 109.

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